NOTICE AND DISCLAIMER

$1,750,000,000*
State of California
Various Purpose General Obligation Bonds

Please be advised of the availability of the electronic version of the Preliminary Official Statement dated April 9, 2004 relating to the above-captioned Bonds.

The electronic version of this document was created in Adobe Portable Document Format (PDF) using Adobe Acrobat 6.0, and you will need Adobe Reader software to accurately read and print it. If you do not have the Adobe Reader, or if you are using a version earlier than that used in Adobe Acrobat 6.0, you may obtain an updated version of the Adobe Reader free of charge from the Adobe web site at www.adobe.com. Using software other than the Adobe Reader included in Adobe Acrobat 6.0 may cause the document that you view or print to differ from the Preliminary Official Statement, and you assume the risk of any such discrepancies as well as any discrepancies related to communication transmission, software differences, or other printing problems. A printed copy of this Preliminary Official Statement may be obtained from the Office of the Treasurer of the State of California, P.O. Box 942809, Sacramento, California 94209-0001, telephone (800) 900-3873, or from Jason Wong, Merrill Lynch, Pierce, Fenner & Smith Incorporated, 101 California Street, Suite 1225, San Francisco, California 94105-2829, telephone (415) 676-3204. Investment decisions should only be based upon the Preliminary Official Statement (and the final Official Statement when available), whether in printed form or downloaded using the current Adobe Reader.

The Preliminary Official Statement and information contained therein speak only as of the date written above, and may cease to be accurate after such date. The Preliminary Official Statement is subject to completion, amendment or other change without notice. The posting of the Preliminary Official Statement does not constitute an offer to sell or the solicitation of an offer to buy, nor shall there be any sale of, the Bonds in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of such jurisdiction.

By clicking on the hyperlink at the bottom of this page and accessing the Preliminary Official Statement, you will be deemed to have acknowledged and agreed as follows: (i) you understand and agree to the provisions of this page, (ii) you consent to receive the Preliminary Official Statement in electronic form, (iii) a record will be maintained of your electronic access to the Preliminary Official Statement and of this Notice and Disclaimer, (iv) you agree not to print the Preliminary Official Statement except in its entirety and (v) you will not forward the Preliminary Official Statement to anyone without including the information contained in this Notice and Disclaimer.

(* Preliminary, subject to change.)

VIEW PRELIMINARY OFFICIAL STATEMENT

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$1,750,000,000
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State of California
Various Purpose General Obligation Bonds

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PRELIMINARY OFFICIAL STATEMENT

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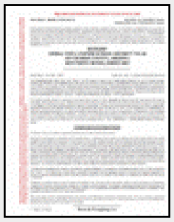

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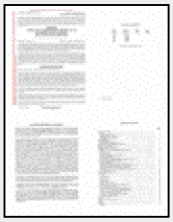

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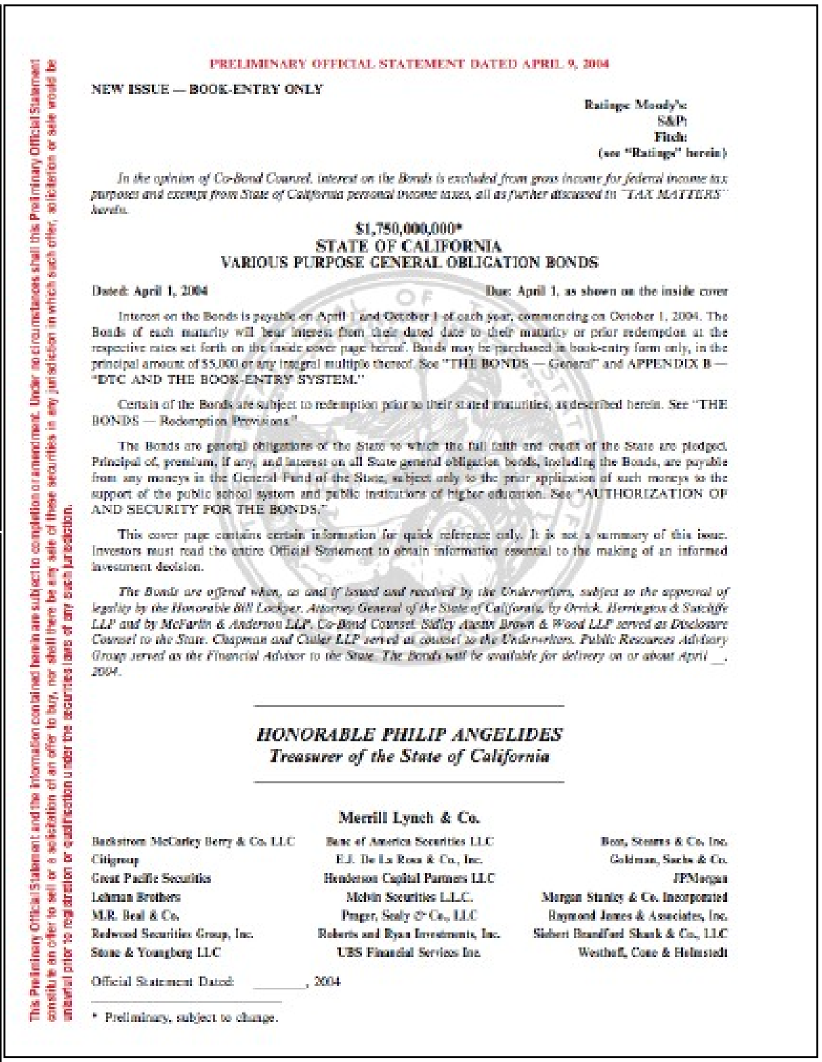

PRELIMINARY OFFICIAL STATEMENT DATED APRIL 9, 2004

NEW ISSUE — BOOK-ENTRY ONLY

Ratings: Moody's:
S&P:
Fitch:
(see "Ratings" herein)

In the opinion of Co-Bond Counsel, interest on the Bonds is excluded from gross income for federal income tax purposes and exempt from State of California personal income taxes, all as further discussed in "TAX MATTERS" herein.

$1,750,000,000*
STATE OF CALIFORNIA
VARIOUS PURPOSE GENERAL OBLIGATION BONDS

Dated: April 1, 2004 — Due: April 1, as shown on the inside cover

Interest on the Bonds is payable on April 1 and October 1 of each year, commencing on October 1, 2004. The Bonds of each maturity will bear interest from their dated date to their maturity or prior redemption at the respective rates set forth on the inside cover page hereof. Bonds may be purchased in book-entry form only, in the principal amount of $5,000 or any integral multiple thereof. See "THE BONDS — General" and APPENDIX B — "DTC AND THE BOOK-ENTRY SYSTEM."

Certain of the Bonds are subject to redemption prior to their stated maturities, as described herein. See "THE BONDS — Redemption Provisions."

The Bonds are general obligations of the State to which the full faith and credit of the State are pledged. Principal of, premium, if any, and interest on all State general obligation bonds, including the Bonds, are payable from any moneys in the General Fund of the State, subject only to the prior application of such moneys to the support of the public school system and public institutions of higher education. See "AUTHORIZATION OF AND SECURITY FOR THE BONDS."

This cover page contains certain information for quick reference only. It is not a summary of this issue. Investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision.

The Bonds are offered when, as and if issued and received by the Underwriters, subject to the approval of legality by the Honorable Bill Lockyer, Attorney General of the State of California, by Orrick, Herrington & Sutcliffe LLP and by McFarlin & Anderson LLP, Co-Bond Counsel. Sidley Austin Brown & Wood LLP served as Disclosure Counsel to the State. Chapman and Cutler LLP served as counsel to the Underwriters. Public Resources Advisory Group served as the Financial Advisor to the State. The Bonds will be available for delivery on or about April __, 2004.

HONORABLE PHILIP ANGELIDES
Treasurer of the State of California

Merrill Lynch & Co.

Backstrom McCarley Berry & Co. LLC	Banc of America Securities LLC	Bear, Stearns & Co. Inc.
Citigroup	E.J. De La Rosa & Co., Inc.	Goldman, Sachs & Co.
Great Pacific Securities	Henderson Capital Partners LLC	JPMorgan
Lehman Brothers	Melvin Securities L.L.C.	Morgan Stanley & Co. Incorporated
M.R. Beal & Co.	Prager, Sealy & Co., LLC	Raymond James & Associates, Inc.
Redwood Securities Group, Inc.	Roberts and Ryan Investments, Inc.	Siebert Brandford Shank & Co., LLC
Stone & Youngberg LLC	UBS Financial Services Inc.	Westhoff, Cone & Holmstedt

Official Statement Dated: ________, 2004

* Preliminary, subject to change.

This Preliminary Official Statement and the information contained herein are subject to completion or amendment. Under no circumstances shall this Preliminary Official Statement constitute an offer to sell or a solicitation of an offer to buy, nor shall there be any sale of these securities in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such jurisdiction.

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PRELIMINARY OFFICIAL STATEMENT DATED APRIL 9, 2004

NEW ISSUE — BOOK-ENTRY ONLY

Ratings: Moody's:
S&P:
Fitch:
(see "Ratings" herein)

In the opinion of Co-Bond Counsel, interest on the Bonds is excluded from gross income for federal income tax purposes and exempt from State of California personal income taxes, all as further discussed in "TAX MATTERS" herein.

$1,750,000,000*
STATE OF CALIFORNIA
VARIOUS PURPOSE GENERAL OBLIGATION BONDS

Dated: April 1, 2004 **Due: April 1, as shown on the inside cover**

Interest on the Bonds is payable on April 1 and October 1 of each year, commencing on October 1, 2004. The Bonds of each maturity will bear interest from their dated date to their maturity or prior redemption at the respective rates set forth on the inside cover page hereof. Bonds may be purchased in book-entry form only, in the principal amount of $5,000 or any integral multiple thereof. See "THE BONDS — General" and APPENDIX B — "DTC AND THE BOOK-ENTRY SYSTEM."

Certain of the Bonds are subject to redemption prior to their stated maturities, as described herein. See "THE BONDS — Redemption Provisions."

The Bonds are general obligations of the State to which the full faith and credit of the State are pledged. Principal of, premium, if any, and interest on all State general obligation bonds, including the Bonds, are payable from any moneys in the General Fund of the State, subject only to the prior application of such moneys to the support of the public school system and public institutions of higher education. See "AUTHORIZATION OF AND SECURITY FOR THE BONDS."

This cover page contains certain information for quick reference only. It is not a summary of this issue. Investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision.

The Bonds are offered when, as and if issued and received by the Underwriters, subject to the approval of legality by the Honorable Bill Lockyer, Attorney General of the State of California, by Orrick, Herrington & Sutcliffe LLP and by McFarlin & Anderson LLP, Co-Bond Counsel. Sidley Austin Brown & Wood LLP served as Disclosure Counsel to the State. Chapman and Cutler LLP served as counsel to the Underwriters. Public Resources Advisory Group served as the Financial Advisor to the State. The Bonds will be available for delivery on or about April __, 2004.

HONORABLE PHILIP ANGELIDES
Treasurer of the State of California

Merrill Lynch & Co.

Backstrom McCarley Berry & Co. LLC	**Banc of America Securities LLC**	**Bear, Stearns & Co. Inc.**
Citigroup	**E.J. De La Rosa & Co., Inc.**	**Goldman, Sachs & Co.**
Great Pacific Securities	**Henderson Capital Partners LLC**	**JPMorgan**
Lehman Brothers	**Melvin Securities L.L.C.**	**Morgan Stanley & Co. Incorporated**
M.R. Beal & Co.	**Prager, Sealy & Co., LLC**	**Raymond James & Associates, Inc.**
Redwood Securities Group, Inc.	**Roberts and Ryan Investments, Inc.**	**Siebert Brandford Shank & Co., LLC**
Stone & Youngberg LLC	**UBS Financial Services Inc.**	**Westhoff, Cone & Holmstedt**

Official Statement Dated: ________, 2004

* Preliminary, subject to change.

$1,750,000,000*
STATE OF CALIFORNIA
VARIOUS PURPOSE GENERAL OBLIGATION BONDS

MATURITIES, PRINCIPAL AMOUNTS, INTEREST RATES, PRICES AND YIELDS
Base CUSIP:**

Maturity Date (April 1)*	Principal Amount*	Interest Rate	Price or Yield	CUSIP**	Maturity Date (April 1)*	Principal Amount*	Interest Rate	Price or Yield	CUSIP**
2005	$35,000,000				2015	$12,500,000			
2006	35,000,000				2016	12,500,000			
2007	35,000,000				2017	12,500,000			
2008	40,000,000				2018	12,500,000			
2009	40,000,000				2019	12,500,000			
2010	40,000,000				2020	12,500,000			
2011	40,000,000				2021	12,500,000			
2012	40,000,000				2022	12,500,000			
2013	30,000,000				2023	81,465,000			
2014	20,000,000				2024	85,495,000			

$282,640,000* ____% Term Bonds due April 1, 2027* — Yield ____%; CUSIP **________

$845,400,000* ____% Term Bonds due April 1, 2034* — Yield ____%; CUSIP **________

* Preliminary, subject to change. Maturity schedule may be adjusted at pricing.

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Copies of this Official Statement may be obtained from:

HONORABLE PHILIP ANGELIDES
Treasurer of the State of California
P.O. Box 942809
Sacramento, California 94209-0001
1-800-900-3873

This Preliminary Official Statement is available as public information on the State Treasurer's Internet site at http://www.treasurer.ca.gov

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OFFICIAL STATEMENT

$1,750,000,000*
STATE OF CALIFORNIA
VARIOUS PURPOSE GENERAL OBLIGATION BONDS

INTRODUCTION

This Introduction contains only a brief summary of the terms of the Bonds and a brief description of the Official Statement; a full review should be made of the entire Official Statement, including the Appendices and the financial statements incorporated by reference. Summaries of provisions of the Constitution and laws of the State of California or any other documents referred to in this Official Statement do not purport to be complete and such summaries are qualified in their entirety by references to the complete provisions.

Description of the Bonds

This Official Statement presents certain information relating to the State of California (the "State") in connection with the sale of general obligation bonds in the aggregate principal amount of $1,750,000,000* (the "Bonds"). The Bonds are described further below under "THE BONDS—Identification and Authorization of the Bonds."

The Bonds will be registered in the name of a nominee of The Depository Trust Company, New York, New York ("DTC"), which will act as securities depository for the Bonds. Beneficial interests in the Bonds may be purchased in book-entry form only, in denominations of $5,000 or any integral multiple thereof. See "THE BONDS – General" and APPENDIX B – "DTC AND THE BOOK-ENTRY SYSTEM."

The Bonds are authorized by Bond Acts (defined in "AUTHORIZATION OF AND SECURITY FOR THE BONDS – Authorization") approved by the voters of the State and by resolutions of finance committees (the "Resolutions") created under the Bond Acts. The Bonds are being issued to repay interim loans from the State's Pooled Money Investment Account that financed construction of various projects under the respective Bond Acts, to finance various projects under the respective Bond Acts and to pay certain costs of issuance of the Bonds. See "THE BONDS – Purposes of the Bonds."

Security and Source of Payment for the Bonds

The Bonds are general obligations of the State to which the full faith and credit of the State are pledged. See "AUTHORIZATION OF AND SECURITY FOR THE BONDS – Security." Principal of, premium, if any, and interest on all State general obligation bonds, including the Bonds, are payable from moneys in the General Fund of the State Treasury (the "General Fund") subject only to the prior application of moneys in the General Fund to the support of the public school system and public institutions of higher education. See APPENDIX A – "THE STATE OF CALIFORNIA – STATE FINANCES – The General Fund" and – "STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Capital Facilities Financing – General Obligation Bonds." The Bond Acts authorizing the Bonds provide that the State shall collect annually, in the same manner and at the same time as it collects other State revenues, a sum sufficient, in addition to the ordinary revenues of the State, to pay the principal of and interest on the Bonds.

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* Preliminary, subject to change.

Redemption

The Bonds of certain maturities will be subject to optional redemption prior to their respective stated maturity dates, in whole or in part, and to mandatory redemption prior to their respective stated maturities, in part, from sinking fund payments made by the State. See "THE BONDS – Redemption Provisions."

Information Related to this Official Statement

The information set forth herein has been obtained from official sources that are believed to be reliable, but is not guaranteed as to accuracy or completeness. The information and expressions of opinion herein are subject to change without notice, and neither delivery of this Official Statement nor any sale made hereunder or any future use of this Official Statement shall, under any circumstances, create any implication that there has been no change in the affairs of the State since the date hereof.

All financial and other information presented or incorporated by reference in this Official Statement has been provided by the State from its records, except for information expressly attributed to other sources. The presentation of certain information, including tables of receipts from taxes and other revenues, is intended to show recent historic information and is not intended to indicate future or continuing trends in the financial position or other affairs of the State. No representation is made that past experience, as it might be shown by such financial and other information, will necessarily continue or be repeated in the future. However, certain statements included or incorporated by reference in this Official Statement do constitute "forward-looking statements." Such statements are generally identifiable by the terminology used such as "plan," "expect," "estimate," "budget" or other similar words. The achievement of certain results or other expectations contained in such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements described to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. The State does not plan to issue any updates or revisions to those forward-looking statements if or when its expectations or events, conditions or circumstances on which such statements are based occur. Any statements made in this Official Statement involving matters of opinion, whether expressly stated or not, are set forth as such and not as representations of fact.

A wide variety of other information, including financial information, concerning the State is available from State agencies, State agency publications and State agency websites. Any such information that is inconsistent with the information set forth in this Official Statement should be disregarded. No such information is a part of or incorporated into this Official Statement, except as expressly noted in APPENDIX A – "THE STATE OF CALIFORNIA – FINANCIAL STATEMENTS."

The information in APPENDIX B – "DTC AND THE BOOK-ENTRY SYSTEM" has been furnished by DTC and no representation is made by the State, the Financial Advisor or the Underwriters as to the accuracy or completeness of such information.

No dealer, broker, salesperson or other person has been authorized by the State to give any information or to make any representations other than those contained herein and, if given or made, such other information or representations must not be relied upon as having been authorized by the State. This Official Statement is not to be construed as a contract with the purchasers of the Bonds.

The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as part of, their responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction. In connection with the offering of the Bonds, the Underwriters may over-allot or effect transactions which stabilize or maintain the market price of the Bonds offered hereby at levels above those which might otherwise prevail in the open market. Such stabilizing, if commenced, may be discontinued at any time. The Underwriters may offer and sell the Bonds to certain dealers, institutional investors and others at prices lower than the public offering prices stated on the inside cover hereof, and said public offering may be changed from time to time by the Underwriters.

This Official Statement does not constitute an offer to sell the Bonds or the solicitation of an offer to buy, nor shall there be any sale of, the Bonds by any person in any state or other jurisdiction to any person to whom it is unlawful to make such offer, solicitation or sale in such state or jurisdiction.

Continuing Disclosure

The State Treasurer will agree on behalf of the State to provide annually certain financial information and operating data relating to the State by not later than April 1 of each year in which any Bonds are outstanding (the "Annual Report"), commencing with the report containing 2003-2004 Fiscal Year financial information, and to provide notice of the occurrence of certain enumerated events if material. The specific nature of the information to be contained in the Annual Report and the notices of material events and certain other terms of the continuing disclosure obligation are set forth in APPENDIX C – "FORM OF CONTINUING DISCLOSURE CERTIFICATE."

The State has not failed to comply, in all material respects, with any "previous undertakings," as that term is used in Rule 15c2-12 (the "Rule") promulgated under the Securities and Exchange Act of 1934, as amended.

AUTHORIZATION OF AND SECURITY FOR THE BONDS

Authorization

Each general obligation bond act authorizing the issuance of the Bonds (collectively, the "Bond Acts") incorporates by reference the State General Obligation Bond Law (the "Law") in Chapter 4 (commencing with Section 16720) of Part 3 of Division 4 of Title 2 of the California Government Code. The Law provides for the authorization, sale, issuance, use of proceeds, repayment and refunding of State general obligation bonds.

Security

The Bonds are general obligations of the State, payable in accordance with the Bond Acts out of the General Fund. The Bond Acts provide that the State will collect annually in the same manner and at the same time as it collects other State revenue an amount sufficient, in addition to the ordinary revenue of the State, to pay principal of and interest on the Bonds. The Bond Acts also contain a continuing appropriation from the General Fund of the sum annually necessary to pay the principal of and interest on the Bonds as they become due and payable. It is an event of default of the State to fail to pay or to fail to caused to be paid the principal of or interest on the Bonds when due or to declare a moratorium on the payment of, or to repudiate any Bond.

The full faith and credit of the State are pledged for the punctual payment of the principal of and the interest on the Bonds. All payments of principal of, premium, if any, and interest on all State general obligation bonds, including the Bonds, have an equal claim to the General Fund, subject only to the prior application of moneys in the General Fund to the support of the public school system and public institutions of higher education. Payment of principal of and interest on the Bonds has a higher priority than the payment of any short term borrowings of the State, including the repayment of $13.965 billion of short term borrowings which are due in June 2004 (and the repayment of the financial institutions which have provided credit support for some of those short term borrowings).

In the event that the State is required to draw upon the credit support facilities to pay its outstanding short term borrowings, the State's ability to manage its daily cash flow will be severely restricted, as described in Appendix A. See APPENDIX A – "THE STATE OF CALIFORNIA – STATE FINANCES – The General Fund," – "STATE FINANCES – State Warrants," – "STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Capital Facilities Financing – General Obligation Bonds," – "STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Cash Flow Borrowings" and – "CASH FLOW." As further described in Appendix A, the State expects to retire or refinance these short term borrowings with available cash and with the proceeds of economic recovery bonds or, if necessary, other short term borrowings, without drawing upon its available credit support facilities. See APPENDIX A – "THE STATE OF CALIFORNIA – STATE INDEBTEDNESS AND OTHER OBLIGATIONS" – Economic Recovery Bonds."

Remedies

It is an event of default of the State under the Resolutions authorizing Bonds pursuant to the respective Bond Acts to fail to pay or to fail to cause to be paid, when due, or to declare a moratorium on the payment of, or to repudiate any Bond.

In the case one or more events of default occurs, then and in every such case the registered Bondholder is entitled to proceed to protect and enforce such registered Bondholder's rights by such appropriate judicial proceeding as such registered Bondholder deems most effectual to protect and enforce any such right, whether by mandamus or other suit or proceeding at law or in equity, for the specific performance of any covenant or agreement contained in the Resolutions authorizing Bonds, as more specifically set forth in each Resolution authorizing Bonds pursuant to the respective Bond Acts. Beneficial Owners of the Bonds (the "Beneficial Owners") cannot protect and enforce such rights except through the registered Bondholder. See, "THE BONDS – General," and APPENDIX B –"DTC AND THE BOOK-ENTRY SYSTEM."

THE BONDS

General

The Bonds will be registered in the name of a nominee of DTC, which will act as securities depository for the Bonds. Beneficial interests in the Bonds may be purchased in book-entry form only in denominations of $5,000 or any integral multiple thereof. See APPENDIX B – "DTC AND THE BOOK-ENTRY SYSTEM." The information in APPENDIX B – "DTC AND THE BOOK-ENTRY SYSTEM" has been furnished by DTC and no representation is made by the State, the Financial Advisor or the Underwriters as to the accuracy or completeness of such information.

Neither the State Treasurer nor the Underwriters can and does give any assurances that DTC will distribute to Participants, or that Participants or others will distribute to the Beneficial Owners, payment of principal of and interest on the Bonds paid or any redemption or other notices or that they will do so on a timely basis or will serve and act in the manner described in this Official Statement. Neither the State Treasurer nor the Underwriters is responsible or liable for the failure of DTC or any Direct Participant or Indirect Participant to make any payments or give any notice to a Beneficial Owner with respect to the Bonds or any error or delay relating thereto.

The Bonds will be dated April 1, 2004 and will mature on April 1 of the years and in the amounts set forth on the inside cover page hereof. Interest on the Bonds is payable on April 1 and October 1 in each year (each, an "Interest Payment Date), commencing on October 1, 2004, at the rates shown on the inside cover page of this Official Statement. Interest on the Bonds will be calculated on the basis of a 360-day year comprising twelve 30-day months.

Principal and interest are payable directly to DTC by the State Treasurer. Upon receipt of payments of principal and interest, DTC is to in turn remit such principal and interest to the Participants in DTC for disbursement to the Beneficial Owners of the Bonds. The record date for the payment of interest on the Bonds is the close of business on the 15th day of the month immediately preceding an Interest Payment Date, whether or not the record date falls on a business day.

Identification and Authorization of the Bonds

The Bonds are being issued as six separate series to finance various projects authorized by the voters pursuant to the four separate Bond Acts as set forth below.

$__________ principal amount of State of California Class Size Reduction Kindergarten-University Public Education Facilities Bonds, Series AT, authorized by the State School Building Finance Committee under the Class Size Reduction Kindergarten-University Public Education Facilities Bond Act of 1998.

$__________ principal amount of State of California Class Size Reduction Kindergarten-University Public Education Facilities Bonds, Series AU, authorized by the Higher Education Facilities Finance Committee under the Class Size Reduction Kindergarten-University Public Education Facilities Bond Act of 1998.

$______ principal amount of State of California Kindergarten-University Public Education Facilities Bonds, Series G, authorized by the Higher Education Facilities Finance Committee under the Kindergarten-University Public Education Facilities Bond Act of 2002.

$______ principal amount of State of California Kindergarten-University Public Education Facilities Bonds, Series H, authorized by the State School Building Finance Committee under the Kindergarten-University Public Education Facilities Bond Act of 2002.

$__________ principal amount of State of California New Prison Construction Bonds, Series AA, authorized by the 1986 Prison Construction Committee under the New Prison Construction Bond Act of 1986.

$______ principal amount of State of California Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Bonds, Series J, authorized by the Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Finance Committee under the Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Act.

Purposes of the Bonds

The Bonds are being issued to repay interim loans from the State's Pooled Money Investment Account that financed construction of various projects under the respective Bond Acts, to finance various projects under the respective Bond Acts, and to pay certain costs of issuance of the Bonds.

Redemption Provisions

Optional Redemption of Bonds

The Bonds maturing on or before April 1, 20__ are not subject to optional redemption prior to their respective maturities. The Bonds maturing on or after April 1, 20__ are subject to optional redemption prior to their respective stated maturity dates, in whole or in part, in such order of maturity as may be designated by the State Treasurer and by lot within any maturity, on any date on or after April 1, 20__ at a redemption price equal to 100% of the principal amount thereof, plus accrued interest to the date fixed for redemption.

Sinking Fund Redemption

The Bonds maturing on April 1, 20__ (each, the "Term Bonds") are subject to redemption prior to their stated maturity date, in part, by lot, from sinking fund payments made by the State, at a redemption price of 100% of the principal amount thereof plus accrued interest to the sinking fund payment date fixed for redemption, without premium, on April 1 of the years, and in the amounts shown below:

Term Bonds Due April 1, 20__

Sinking Fund Payment Date (April 1)	**Principal Amount Redeemed**
	$

* Maturity date.

If a Term Bond is called for optional redemption in part (see "Optional Redemption of Bonds" above), the remaining sinking fund installments for such Term Bonds shall be adjusted as determined by the State Treasurer.

Notice of Redemption

When redemption is required while the Bonds are in book-entry form, the State Treasurer is to give notice of redemption by mailing copies of such notice only to DTC (not to the Beneficial Owners of the Bonds) not less than 30 or more than 60 days prior to the date fixed for redemption. DTC, in turn, is to send the notice of redemption to its participants for distribution to the Beneficial Owners of the Bonds. See APPENDIX B - "DTC AND THE BOOK-ENTRY SYSTEM." The notice from the State Treasurer will state, among other things, that the Bonds or a designated portion thereof (in the case of partial redemption of a Bond) are to be redeemed, the dated date of the Bonds, the date fixed for redemption, the maturities of the Bonds to be redeemed and the redemption price. The notice will also state that after the date fixed for redemption, no further interest will accrue on the principal of any Bonds called for redemption. Notice of redemption will also be provided by mail to certain financial information services and securities depositories.

Annual Debt Service Requirements

The following table sets forth the amounts required to be made available for the payment of principal (whether at maturity or by sinking fund payments), interest and the total payments due on the Bonds.

Fiscal Year Ended June 30	Principal	Interest	Fiscal Year Total Debt Service
	$	$	$
Total	$	$	$

LEGAL MATTERS

The opinion of the Honorable Bill Lockyer, Attorney General of the State of California (the "Attorney General"), approving the validity of the Bonds will accompany the Bonds deposited with DTC. The opinions of Orrick, Herrington & Sutcliffe LLP and McFarlin & Anderson LLP, Co-Bond Counsel, approving the validity of the Bonds and addressing certain tax matters will also accompany the Bonds deposited with DTC. The proposed forms of legal opinions for the Bonds are set forth in APPENDIX D. See "TAX MATTERS" and APPENDIX D – "PROPOSED FORMS OF LEGAL OPINIONS." Sidley Austin Brown & Wood LLP served as Disclosure Counsel to the State. Chapman and Cutler LLP served as counsel to the Underwriters.

The Attorney General, Co-Bond Counsel, Disclosure Counsel and Underwriters' Counsel, respectively, undertake no responsibility for the accuracy, completeness or fairness of this Official

Statement, except as otherwise stated in their respective opinions delivered upon the issuance of the Bonds; none of such opinions is addressed to or intended to be relied upon by purchasers of the Bonds.

TAX MATTERS

In the opinion of Orrick, Herrington & Sutcliffe LLP and McFarlin & Anderson LLP, Co-Bond Counsel, based upon an analysis of existing laws, regulations, rulings, and court decisions, and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest on the Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, as amended, (the "Code") and is exempt from State of California personal income taxes. Co-Bond Counsel are of the further opinion that such interest is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Co-Bond Counsel observe that such interest is included in adjusted current earnings when calculating federal corporate alternative minimum taxable income. A complete copy of the proposed form of opinions of Co-Bond Counsel is set forth in APPENDIX D – "PROPOSED FORMS OF LEGAL OPINIONS."

The amount (if any) by which the issue price of the Bonds of any given maturity is less than the amount to be paid on such date (excluding amounts stated to be interest and payable at least annually over term of such Bonds) constitutes "original issue discount," the accrual of which, to the extent properly allocable to each owner thereof, is treated as interest on the Bonds which is excluded from gross income for federal income tax purposes and which is exempt from State of California personal income taxes. For this purpose, the issue price of a particular maturity of the Bonds is the first price at which a substantial amount of such maturity of the Bonds is sold to the public (excluding bond houses, brokers, or similar persons or organizations acting in the capacity of underwriters, placement agents or wholesalers). The original issue discount with respect to Bonds of any maturity date accrues daily over the term to such maturity date on the basis of a constant interest rate compounded semiannually (with straight-line interpolations between compounding dates). The accruing original issue discount is added to the adjusted basis of such Bonds to determine taxable gain or loss upon disposition (including sale, redemption, or payment on maturity) of such Bonds. Beneficial Owners of the Bonds should consult their own tax advisors with respect to the tax consequences of ownership of Bonds with original issue discount, including the treatment of purchasers who do not purchase such Bonds in the original offering to the public at the first price which a substantial amount of such Bonds is sold to the public.

Any Bonds purchased, whether at original issuance or otherwise, for an amount greater than their principal amount payable at maturity (or, in some cases, at their earlier call date) ("Premium Bonds") will be treated as having amortizable bond premium. No deduction is allowable for the amortizable bond premium in the case of obligations, like the Premium Bonds, the interest on which is excluded from gross income for federal income tax purposes. However, the amount of tax-exempt interest received and a purchaser's basis in a Premium Bond, will be reduced by the amount of amortizable bond premium properly allocable to such purchaser. Beneficial Owners of Premium Bonds should consult their own tax advisors with respect to the proper treatment of amortizable bond premium in their particular circumstances.

The Code imposes various restrictions, conditions and requirements relating to the exclusion from gross income for federal income tax purposes of interest on obligations such as the Bonds. The State has made certain representations and covenanted to comply with certain restrictions, conditions, and requirements designed to ensure that interest on the Bonds will not be included in federal gross income. Inaccuracy of these representations or failure to comply with these covenants may result in interest on the Bonds being included in gross income for federal income tax purposes, possibly from the date of original delivery of the Bonds. The opinions of Co-Bond Counsel assume compliance with these covenants.

Co-Bond Counsel have not undertaken to determine (or to inform any person) whether any actions taken (or not taken) or events occurring (or not occurring) or any other matters coming to the attention of Co-Bond Counsel after the date of delivery of the Bonds may adversely affect the value of, or the tax status of interest on, the Bonds.

Although Co-Bond Counsel are of the opinion that interest on the Bonds is excluded from gross income for federal income tax purposes and is exempt from State of California personal income taxes, the ownership or disposition of, or the accrual or receipt of interest on, the Bonds may otherwise affect a beneficial owner's federal or state tax liability. The nature and extent of these other tax consequences will depend upon the particular tax status of the beneficial owner or the beneficial owner's other items of income or deduction. Co-Bond Counsel express no opinion regarding any such other tax consequences.

Future legislation, if enacted into law, or clarification of the Code, may cause interest on the Bonds to be subject, directly or indirectly, to federal income taxation, or otherwise prevent Owners of the Bonds from realizing the full current benefit of the tax status of such interest. The introduction or enactment of any such future legislation or clarification of the Code may also affect the market price for, or marketability of, the Bonds. Prospective purchasers of the Bonds should consult their own tax advisers regarding any pending or proposed federal tax legislation, as to which Co-Bond Counsel expresses no opinion.

The opinion of Co-Bond Counsel is based on current legal authority, covers certain matters not directly addressed by such authorities, and represents Co-Bond Counsel's judgment as to the proper treatment of the Bonds for federal income tax purposes. It is not binding on the Internal Revenue Service ("IRS") or the courts. Co-Bond Counsel cannot give and has not given any opinion or assurance about the future activities of the State, or about the effect of future changes in the Code, the applicable regulations, the interpretation thereof or changes in enforcement thereof by the IRS. The State has covenanted, however, to comply with the requirements of the Code.

Co-Bond Counsel's engagement with respect to the Bonds ends with the issuance of the Bonds, and, unless separately engaged, Co-Bond Counsel is not obligated to defend the State regarding the tax-exempt status of the Bonds in the event of an audit examination by the IRS. Under current procedures, parties other than the State and their appointed counsel, including the Beneficial Owners, would have little if any right to participate in the audit examination process. Moreover, because achieving judicial review in connection with an audit examination of tax-exempt bonds is difficult, obtaining an independent review of IRS positions with which the State legitimately disagrees, may not be practicable. Any action of the IRS, including but not limited to selection of the Bonds for audit, or the course or result of such audit, or an audit of bonds presenting similar tax issues may affect the market price for, or the marketability of, the Bonds, and may cause the State or the Beneficial Owners to incur significant expense.

LITIGATION

The Attorney General has advised that, to the best of his knowledge, no litigation is now pending (with service of process against the State having been accomplished) or threatened seeking to restrain or enjoin the sale, issuance, execution or delivery of the Bonds or challenging the validity of the Bonds or any proceedings or authority under which the Bonds are being issued.

At any given time, including the present, there are numerous civil actions pending against the State that could, if determined adversely to the State, affect the State's expenditures and, in some cases, its revenues and cash flow. While there can be no assurances as to the ultimate outcome and fiscal impact of such litigation, the State believes that it is unlikely that the outcome of such litigation will adversely affect the ability of the State to pay the principal of and interest on the Bonds when due. See APPENDIX A — "THE STATE OF CALIFORNIA — CASH FLOW, — "CURRENT STATE BUDGET" and — "LITIGATION."

FINANCIAL STATEMENTS

Audited General Purpose Financial Statements of the State of California for the Fiscal Year ended June 30, 2003 (the "Financial Statements") are available. Such Financial Statements have been filed with all of the Nationally Recognized Municipal Securities Information Repositories, as part of an Official Statement relating to the $186,110,000 State Public Works Board Lease Revenue Refunding Bonds (Department of Corrections), Series D and $93,975,000 of State Public Works Board Lease Revenue Refunding Bonds (Department of Corrections), Series E issued in March 2004. The Financial Statements are incorporated by reference into this Preliminary Official Statement. The Financial Statements are also available through electronic means. No such information is a part of or incorporated into this Official Statement, except as expressly noted in APPENDIX A – "THE STATE OF CALIFORNIA – FINANCIAL STATEMENTS." Certain unaudited financial information for the eight months ended February 29, 2004 is included as Exhibit 1 to Appendix A. See APPENDIX A – "EXHIBIT 1 STATE CONTROLLER'S STATEMENT OF GENERAL FUND CASH RECEIPTS AND DISBURSEMENTS, JULY 1, 2003 THROUGH FEBRUARY 29, 2004 (UNAUDITED)."

RATINGS

The Bonds have received ratings of "___" by Moody's Investors Service ("Moody's"), "___" by Standard & Poor's, a Division of The McGraw-Hill Companies, Inc. ("S&P"), and "___" by Fitch Ratings ("Fitch"). An explanation of the significance and status of such credit ratings may be obtained from the rating agencies furnishing the same. There is no assurance that such ratings will continue for any given period of time or that they will not be revised or withdrawn entirely by any such rating agencies if, in their respective judgments, circumstances so warrant. Any revision or withdrawal of a credit rating could have an effect on the market prices and marketability of the Bonds. The State can not predict the timing or impact of future actions by the rating agencies. See "APPENDIX A – INTRODUCTION – California's Credit History."

After the Bonds are rated, the State Treasurer intends to provide appropriate periodic credit information to the rating agencies.

FINANCIAL ADVISOR

Public Resources Advisory Group served as the Financial Advisor to the State in connection with the issuance of the Bonds.

UNDERWRITING

The Underwriters have agreed to purchase the Bonds at a purchase price of $__________ (which amount represents the principal amount of the Bonds in the amount of $_________, less original issue discount of $_________, plus original issue premium of $_________, less Underwriters' compensation in the amount of $__________ and plus accrued interest of $_________). The public offering prices may be changed from time to time by the Underwriters.

CERTAIN AFFILIATIONS

Affiliates of a number of the Underwriters of the Bonds have also provided credit support facilities for one or more of the State's outstanding short-term borrowings.

ADDITIONAL INFORMATION

The State Treasurer will execute a certificate upon delivery of the Bonds to the effect that, to the best of the State Treasurer's knowledge, information and belief, as of the delivery date, the information and statements contained in this Official Statement are complete, true and correct in all material respects and does not contain any untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements therein, in the light of the circumstances under which they were made, not misleading.

STATE OF CALIFORNIA
PHILIP ANGELIDES
Treasurer of the State of California

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APPENDIX A

THE STATE OF CALIFORNIA

Honorable Philip Angelides
Treasurer of the State of California

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INTRODUCTION TO APPENDIX A

Importance of APPENDIX A. APPENDIX A is the part of the Official Statement that provides investors with information concerning the State of California. Investors must read the entire Official Statement, including APPENDIX A, to obtain information essential to making an informed investment decision.

Election of New Governor. At a special election held on October 7, 2003, the Governor of the State, Gray Davis, was recalled and replaced by Arnold Schwarzenegger. Since taking office on November 17, 2003, Governor Schwarzenegger rescinded the suspension of vehicle license fee offsets, proposed a bond measure (Proposition 57) that would authorize the issuance of economic recovery bonds to finance the negative General Fund reserve balance as of June 30, 2004, and other General Fund obligations undertaken prior to June 30, 2004, and proposed a Constitutional amendment (Proposition 58) that would require the State to adopt and maintain a balanced budget, establish a reserve, and restrict future long-term deficit related borrowing. The bond measure and the Constitutional amendment were both adopted at the March 2, 2004 statewide primary election. See "RECENT DEVELOPMENTS REGARDING STATE ECONOMY AND FINANCES."

Payment Priority of General Obligation Bonds. The Bonds are general obligations of the State to which the full faith and credit of the State are pledged. Principal of, premium, if any, and interest on all State general obligation bonds, including the Bonds, are payable from any moneys in the General Fund of the State, subject only to the prior application of such moneys to the support of the public school system and public institutions of higher education.

Payment of principal and interest on the State's general obligation bonds has a higher priority than the payment of any short-term borrowings of the State, including the repayment of $13.965 billion of short-term borrowings which are due in June, 2004 (and the repayment of the financial institutions which have provided credit support facilities for some of those borrowings).

In the event the State is required to draw upon the credit support facilities to pay its outstanding short-term borrowings, the State's ability to manage its daily cash flow will be severely restricted. The State expects to retire or refinance these short-term borrowings with available cash and with the proceeds of economic recovery bonds or, if necessary, other short-term borrowings, without drawing upon its available credit support facilities. See "STATE FINANCES – The General Fund," – "State Warrants," – "STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Capital Facilities Financing – General Obligation Bonds," "STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Cash Flow Borrowings" and "CASH FLOW" herein.

California's Credit History. California has always paid the principal of and interest on its general obligation bonds, general obligation commercial paper notes, lease-purchase obligations and short-term obligations, including revenue anticipation notes and revenue anticipation warrants, when due.

In July 2003, Standard & Poor's downgraded the State's general obligation credit rating to "BBB." In December 2003, the State's general obligation credit rating was downgraded to "BBB" by Fitch and "Baa1" by Moody's.

On March 3, 2004, Moody's, which had its rating of the State's general obligation bonds on "negative outlook," changed its outlook to "stable" following the outcome of the elections for Propositions 57 and 58 at the March 2, 2004, statewide primary. As a result of the election, Standard & Poor's has put its general obligation bond rating of the State on credit watch with positive implications. Fitch's rating of the State's general obligation bonds remains on ratings' watch – negative.

Any revisions or withdrawal of a credit rating could have an effect on the market price and liquidity of the Bonds. The State cannot predict the timing or impact of future actions by the rating agencies. See also "RATINGS" in the forepart of this Official Statement.

Overview of APPENDIX A. APPENDIX A begins with a description of recent developments regarding the State's economy and finances and then discusses the types of debt instruments that the State has issued and is authorized to issue in the future. See "RECENT DEVELOPMENTS REGARDING STATE ECONOMY AND FINANCES" and "STATE INDEBTEDNESS AND OTHER OBLIGATIONS." A discussion of the State's current and projected cash flow is contained under "CASH FLOW."

APPENDIX A continues with a discussion of the sources and uses of State funds. See "STATE FINANCES." The budget process and constraints on this process, as well as the budget proposed by the Governor and the economic assumptions underlying the revenue projections contained in the proposed budget, are discussed under "THE BUDGET PROCESS" and "CURRENT STATE BUDGET."

Then, APPENDIX A includes or incorporates by reference the Audited Annual Financial Statements of the State for the Year Ended June 30, 2003, together with certain information required by governmental accounting and financial reporting standards to be included in the Financial Statements, including a "Management's Discussion and Analysis" that describes and analyzes the financial position of the State and provides an overview of the State's activities for the fiscal year ended June 30, 2003. The State Controller's unaudited reports of cash receipts and disbursements for the period July 1, 2003 through February 29, 2004 are also included in this APPENDIX A. See "FINANCIAL STATEMENTS."

Governance, management and employee information is set forth under "OVERVIEW OF STATE GOVERNMENT." Demographic and economic statistical information is included under "ECONOMY AND POPULATION."

APPENDIX A concludes with a description of material litigation involving the State (see "LITIGATION") and debt tables (see "STATE DEBT TABLES").

RECENT DEVELOPMENTS REGARDING STATE ECONOMY AND FINANCES

In recent years, the State has experienced a decline in State revenues attributable in large part to declines in personal income tax receipts including particularly stock market related income tax revenues, such as capital gains realizations and stock option income. The State estimates that stock market related revenue declined from $17.6 billion in fiscal year 2000-01 to $8.6 billion in fiscal year 2001-02, and to $5.2 billion in 2002-03, a total 70 percent decline. Total personal income tax revenue declined from $44.6 billion to $32.7 billion in the same period. The State's economy continued to grow slowly through the end of 2003 but is projected to grow moderately in 2004. See, "CURRENT STATE BUDGET—Economic Assumptions."

The 2004-05 Governor's Budget, released on January 9, 2004, reported that in the absence of structural corrective actions to change existing policies, operating deficits, estimated at $14 billion in 2004-05, would continue to be incurred. See "CURRENT STATE BUDGET—2004-05 Governor's Budget." See also "CURRENT STATE BUDGET—Continuing Structural Deficit."

Two measures intended to address the existing cumulative budget deficit and to implement structural reform were both approved at the March 2, 2004 statewide primary election. The California Economic Recovery Bond Act (Proposition 57) authorizes the issuance of up to $15 billion of economic recovery bonds to finance the negative General Fund reserve balance as of June 30, 2004, and other General Fund obligations undertaken prior to June 30, 2004. The bonds will be issued in lieu of fiscal recovery bonds authorized by the California Fiscal Recovery Financing Act (Government Code Section 99000 *et. seq.*). The Balanced Budget Amendment (Proposition 58) requires the State to adopt and maintain a balanced budget and establish a reserve, and restricts future long-term deficit-related borrowing. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Economic Recovery Bonds, "THE BUDGET PROCESS—General." and "THE BUDGET PROCESS—Constraints on the Budget Process."

On March 4, 2004 over three dozen cities filed a petition for writ of mandate in the Alameda County Superior Court (*City of Cerritos et al. v. State Board of Equalization*) seeking to prohibit the State Board of Equalization from implementing a one-quarter cent reduction in the amount of sales and use tax that may be collected by local governments. See "STATE FINANCES – Sources of Tax Revenue – Sales Tax." This reduction was approved by the Legislature as part of Chapter 2 of the Statues of 2003-04, Fifth Extraordinary Session, which also enacted the California Economic Recovery Bond Act (approved by the electorate as Proposition 57) and a one-quarter cent increase in the State sales and use tax to secure the bonds issued under the California Economic Recovery Bond Act. The petition filed by the cities does not challenge the authorization for the issuance of the economic recovery bonds or the imposition of the temporary one-quarter cent increase in the State sales and use tax. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Economic Recovery Bonds."

STATE INDEBTEDNESS AND OTHER OBLIGATIONS

General

The State Treasurer is responsible for the sale of debt obligations of the State and its various authorities and agencies. The State has always paid the principal of and interest on its general obligation bonds, general obligation commercial paper notes, lease-purchase debt and short-term obligations, including revenue anticipation notes and revenue anticipation warrants, when due.

Capital Facilities Financing

General Obligation Bonds

The State Constitution prohibits the creation of general obligation indebtedness of the State unless a bond measure is approved by a majority of the electorate voting at a general election or a direct primary. General obligation bond acts provide that debt service on general obligation bonds shall be appropriated annually from the General Fund and all debt service on general obligation bonds is paid from the General Fund. Under the State Constitution, debt service on general obligation bonds is the second charge to the General Fund after the application of moneys in the General Fund to the support of the public school system and public institutions of higher education. See "STATE FINANCES—State Expenditures." Certain general obligation bond programs receive revenues from sources other than the sale of bonds or the investment of bond proceeds.

As of March 1, 2004, the State had outstanding $33,298,417,000 aggregate principal amount of long-term general obligation bonds, and unused voter authorizations for the future issuance of $20,221,001,000 of long-term general obligation bonds. This latter figure consists of $11,958,157,000 of general obligation bonds which are authorized by State finance committees to be issued initially as commercial paper notes, described below, and $8,262,844,000 of other authorized but unissued general obligation bonds. See the table "Authorized and Outstanding General Obligation Bonds" under "STATE DEBT TABLES." See introduction to "STATE DEBT TABLES" for information as to bonds issued or expected to be issued after March 1, 2004.

General obligation bond law permits the State to issue as variable rate indebtedness up to 20 percent of the aggregate amount of long-term general obligation bonds outstanding. The State has issued $1.4 billion of variable rate general obligation bonds, representing 4.2% of the State's total outstanding general obligation bonds as of March 1, 2004.

In addition to the $15 billion of economic recovery bonds and the $12.3 billion of Kindergarten-University Public Education Facilities Bonds approved by the voters at the March 2, 2004 election, the Legislature has approved placing a $9.95 billion bond measure (the Safe, Reliable High-Speed Passenger Train Bond Act of the 21st Century) on the ballot in November of 2004. Additional bond proposals may also be added in 2004. See "2004-05 GOVERNOR'S BUDGET—Fiscal Year 2004-05."

Commercial Paper Program

Pursuant to legislation enacted in 1995, voter-approved general obligation indebtedness may be issued either as long-term bonds or, for some but not all bond issues, as commercial paper notes. Commercial paper notes may be renewed or may be refunded by the issuance of long-term bonds. The State issues long-term general obligation bonds from time to time to retire its general obligation commercial paper notes. Commercial paper notes are deemed issued upon authorization by the respective finance committees, whether or not such notes are actually issued. Pursuant to the terms of the bank credit agreement presently in effect supporting the general obligation commercial paper program, not more than $1.46 billion in general obligation commercial paper notes may be outstanding at any time. This amount may be increased or decreased in the future. As of March 1, 2004, the State did not have any General Obligation Commercial Paper Notes outstanding. See "STATE DEBT TABLES."

Lease-Purchase Obligations

In addition to general obligation bonds, the State builds and acquires capital facilities through the use of lease-purchase borrowing. Under these arrangements, the State Public Works Board, another State or local agency or a joint powers authority issues bonds to pay for the construction of facilities such as office buildings, university buildings or correctional institutions. These facilities are leased to a State agency or the University of California under a long-term lease that provides the source of payment of the debt service on the lease-purchase bonds. In some cases, there is not a separate bond issue, but a trustee directly creates certificates of participation in the State's lease obligation, which are then marketed to investors. Under applicable court decisions, such lease arrangements do not constitute the creation of "indebtedness" within the meaning of the State Constitutional provisions that require voter approval. For purposes of this Appendix A and the tables under "STATE DEBT TABLES," "lease-purchase obligation" or "lease-purchase financing" means principally bonds or certificates of participation for capital facilities where the rental payments providing the security are a direct or indirect charge against the General Fund and also includes revenue bonds for a State energy efficiency program secured by payments made by various State agencies under energy service contracts. Certain of the lease-purchase financings are supported by special funds rather than the General Fund. See "STATE FINANCES—Sources of Tax Revenue—Special Fund Revenues." The tables under "STATE DEBT TABLES" do not include equipment leases or leases which were not sold, directly or indirectly, to the public capital markets. The State had $6,873,962,136 General Fund-supported lease-purchase obligations outstanding as of March 1, 2004. The State Public Works Board, which is authorized to sell lease revenue bonds, had $4,260,165,000 authorized and unissued as of March 1, 2004. In addition, as of that date, certain joint powers authorities were authorized to issue approximately $81,000,000 of revenue bonds to be secured by State leases. See introduction to "STATE DEBT TABLES" for information as to bonds issued or expected to be issued after March 1, 2004.

Non-Recourse Debt

Certain State agencies and authorities issue revenue obligations for which the General Fund has no liability. Revenue bonds represent obligations payable from State revenue-producing enterprises and projects, which are not payable from the General Fund, and conduit obligations payable only from revenues paid by private users of facilities financed by the revenue bonds. The enterprises and projects include transportation projects, various public works projects, public and private educational facilities (including the California State University and University of California systems), housing, health facilities and pollution control facilities. State agencies and authorities had $44,390,684,551 aggregate principal amount of revenue bonds and notes which are non–recourse to the General Fund outstanding as of December 31, 2003, as further described in the table "State Agency Revenue Bonds and Conduit Financing" under "STATE DEBT TABLES."

Detailed information regarding the State's long-term debt appears in the section "STATE DEBT TABLES."

Pension Obligation Bonds

Pursuant to the California Pension Obligation Financing Act, Government Code Section 16910 et seq. (the "Pension Bond Act"), the State proposed to issue $1.9 billion of pension obligation bonds to make fiscal year 2003-04 contributions to the California Public Employees' Retirement System ("CalPERS"). The payment of debt service on the pension obligation bonds would be payable from the General Fund subject to the priorities specified in the Pension Bond Act. The proposed pension obligation bonds are the subject of a validation action brought by the Pension Obligation Bond Committee for and on behalf of the State. In that validation action, the Pension Obligation Bond Committee seeks to obtain the court's determination that the pension obligation bonds will not be in violation of the Constitutional debt limit because the proceeds of the pension obligation bonds will be used to pay the State's employer obligation to CalPERS, which is an "obligation imposed by law" and not "debt." On October 2, 2003, the trial court issued a judgment denying the State's request that the bonds be validated. The State is appealing this decision, but it is likely that the courts will not resolve this litigation in time to issue pension obligation bonds in 2003-04. See "LITIGATION—Bond-Related Matters."

The Administration has proposed reforms to the State's pension benefits costs. See "STATE FINANCES—Pension Trusts" and "CURRENT STATE BUDGET—2004-05 Governor's Budget." The Governor has proposed to issue pension obligation bonds to pay a portion of the retirement contributions to CalPERS until the effects of the reforms are sufficiently recognized in CalPERS' actuarial projections. The Administration anticipates that the validation action discussed in the preceding paragraph will be resolved in time to permit the issuance of pension obligation bonds by April 2005. Assuming a favorable decision by the court in the validation matter and authorization of the issuance by the Legislature, the Administration anticipates issuing $929 million of pension obligation bonds to cover the State's April and June 2005 retirement payment obligations. The Administration also estimates that $19.5 million of pension obligation bonds will be issued in 2005-06.

Economic Recovery Bonds

The California Economic Recovery Bond Act ("Proposition 57") was approved by the voters at the statewide primary election on March 2, 2004. Proposition 57 authorizes the issuance of up to $15 billion in economic recovery bonds to finance the negative General Fund reserve balance as of June 30, 2004, and other General Fund obligations undertaken prior to June 30, 2004. Repayment of the economic recovery bonds will be secured by a pledge of revenues from a one-quarter cent increase in the State's sales and use tax starting July 1, 2004. Fifty percent, or up to $5 billion of future deposits in the reserve fund created by the Balanced Budget Amendment ("Proposition 58"), may be used to repay the economic recovery bonds. In addition, as voter-approved general obligation bonds, the economic recovery bonds will be secured by the State's full faith and credit. However, moneys in the General Fund will only be used in the event the dedicated revenue is insufficient to repay the bonds.

The State plans to issue a sufficient amount of economic recovery bonds to provide $12.254 billion of net proceeds to the General Fund in fiscal year 2003-04. The cash flow projections included in the 2004-05 Governor's Budget assume that $12.254 billion of net proceeds from economic recovery bonds will be deposited in the General Fund by June 2004. The State may issue the remainder of authorized economic recovery bonds in future fiscal years. The State's General Obligation Bond Law authorizes the issuance of short-term bond anticipation notes payable from the proceeds of voter-authorized bonds. The State may issue long-term bonds under Proposition 57 or bond anticipation notes followed by takeout long-term bonds, depending upon market conditions and timing requirements.

Enhanced Tobacco Settlement Revenue Bonds

In 1998 the State signed a settlement agreement with the four major cigarette manufacturers. Under the settlement agreement, the cigarette manufacturers agreed to make payments to the State in perpetuity, which payments amount to approximately $25 billion (subject to adjustments) over the first 25 years. Under a separate Memorandum of Understanding, half of the payments made by the cigarette manufacturers will be paid to the State and half to local governments (all counties and the cities of San Diego, Los Angeles, San Francisco and San Jose). The specific amount to be received by the State and local governments is subject to adjustment. Details in the settlement agreement allow reduction of the manufacturers' payments for decreases in cigarette shipment volumes by the settling manufacturers, payments owed to certain "Previously Settled States" and certain types of offsets for disputed payments, among other things. However, settlement payments are adjusted upward each year by at least 3 percent for inflation, compounded annually.

Chapter 414, Statutes of 2002, as amended, allows the issuance of revenue bonds secured by the tobacco settlement revenues received by the State beginning in the 2003-04 fiscal year. An initial sale of

56.57% of the State's tobacco settlement revenues producing $2.5 billion in proceeds was completed in January 2003.

A second sale of the remaining 43.43% of the State's tobacco settlement revenues, which produced $2.264 billion in proceeds, was completed in September 2003. Chapter 414, Statutes of 2002, as amended, requires the Governor to request an appropriation in the annual Budget Act to pay debt service and other related costs of the tobacco settlement revenue bonds secured by the second (and only the second) sale of tobacco settlement revenues when such tobacco settlement revenues are insufficient therefor. The 2003 Budget Act authorized the Director of Finance to make allocations with legislative notification if tobacco settlement revenues are insufficient to cover the cost of the tobacco securitization program in fiscal year 2003-04. The Legislature is not obligated to make any such requested appropriation in the future.

Tobacco settlement revenue bonds are neither general nor legal obligations of the State or any of its political subdivisions and neither the faith and credit nor the taxing power nor any other assets or revenues of the State or of any political subdivision is or shall be pledged to the payment of any such bonds.

Cash Flow Borrowings

As part of its cash management program, the State has regularly issued short-term obligations to meet cash flow needs. The State has issued revenue anticipation notes ("Notes" or "RANs") in 19 of the last 20 fiscal years to partially fund timing differences between revenues and expenditures, as the majority of General Fund revenues are received in the last part of the fiscal year. By law, RANs must mature prior to the end of the fiscal year of issuance. If additional external cash flow borrowings are required, the State has issued revenue anticipation warrants ("RAWs"), which can mature in a subsequent fiscal year. See "STATE FINANCES—State Warrants." RANs and RAWs are both payable from any "Unapplied Money" in the General Fund of the State on their maturity date, subject to the prior application of such money in the General Fund to pay Priority Payments. "Priority Payments" are payments as and when due to: (i) support the public school system and public institutions of higher learning (as provided in Section 8 of Article XVI of the Constitution of the State), (ii) pay principal of (whether at stated maturity or upon earlier redemption) and interest on general obligation bonds of the State, (iii) provide reimbursement from the General Fund to any special fund or account to the extent such reimbursement is legally required to be made to repay borrowings therefrom, and (iv) pay State employees' wages and benefits, State payments to pension and other State employee benefit trust funds, State Medi-Cal claims, and any amounts determined by a court of competent jurisdiction in a final and nonappealable judgment to be required by federal law or the State Constitution to be paid with State warrants that can be cashed immediately. Priority Payments also includes payments of principal and interest on registered warrants issued to make Priority Payments. See "State Finances" below.

The following table shows the amount of RANs and RAWs issued in the past five fiscal years and in the current fiscal year.

TABLE 1
State of California Revenue Anticipation Notes and Warrants Issued
Fiscal Years 1998-99 to 2003-04

Fiscal Year	Type	Principal Amount (Billions)	Date of Issue	Maturity Date
1998-99	Notes	$ 1.70	October 1, 1998	June 30, 1999
1999-00	Notes Series A-B	1.00	October 1, 1999	June 30, 2000
2000-01	No Notes issued			
2001-02	Notes Series A-C	5.70	October 4, 2001	June 28, 2002
	RAWs Series A	1.50	June 24, 2002	October 25, 2002
	RAWs Series B	3.00	June 24, 2002	November 27, 2002
	RAWs Series C	3.00	June 24, 2002	January 30, 2003†
2002-03	Notes Series A and C	6.00	October 16, 2002	June 20, 2003
	Notes Series B and D	3.00	October 16, 2002	June 27, 2003
	Notes Series E – G	3.50	November 6, 2002	June 20, 2003
	RAWs Series A and B	10.965	June 18, 2003	June 16, 2004
2003-04	Notes	3.00	October 28, 2003	June 23, 2004

† Called by the Controller and paid on November 27, 2002.

Source: State of California, Office of the Treasurer.

CASH FLOW

2003 Revenue Anticipation Warrants

On June 18, 2003, the Controller issued $10.965 billion of 2003 Revenue Anticipation Warrants (the "2003 Warrants"), which will mature on June 16, 2004. At the time of issuance, cash flows prepared by the Department of Finance projected that there would be sufficient available moneys in the General Fund (including from internal borrowing) to repay the 2003 Warrants at maturity. Cash flows prepared by the Department of Finance, based upon the 2004-05 Governor's Budget, also project that there will be sufficient available moneys in the General Fund (including from internal borrowing) to repay the 2003 Warrants at maturity. This most recent cash flow projection by the Department of Finance assumed, among other things, the receipt by the State during 2003-04 of $12.254 billion of economic recovery bond proceeds, which were approved by the voters in March 2004. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Economic Recovery Bonds." The payment of principal of and interest on the 2003 Warrants is subject to the prior application of moneys in the General Fund to pay Priority Payments. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Cash Flow Borrowings" for a definition of Priority Payments.

If it appears to the Controller that there will be insufficient available money in the General Fund to pay the 2003 Warrants at maturity, the Controller has agreed to use his best efforts to offer for sale at competitive bid and issue refunding warrants to pay the 2003 Warrants in full. See "STATE FINANCES—State Warrants—Refunding Warrants." While no assurance can be given that the State would be able to sell refunding warrants, the State has always been able to borrow funds to meet its cash flow needs in the past and expects to take all steps necessary to continue to have access to the short-term and long-term credit markets.

If the Controller were unable to issue refunding warrants in sufficient amounts, the State may decide to borrow under seven Forward Warrant Purchase Agreements into which the State has entered with seven financial institutions ("Participants"), on a several and not joint basis (the "Forward Purchase Agreements"), that will enable the State to borrow up to $11.2 billion to obtain additional cash resources to pay the principal of and interest on the 2003 Warrants on their maturity date. The Forward Purchase Agreements do not constitute a guaranty of the 2003 Warrants and contain certain conditions which must be met in order for the State to obtain advances of funds from the Participants. The conditions to be satisfied on June 16, 2004 (the maturity date of the 2003 Warrants), include the condition that no event of default under the Forward Purchase Agreements shall have occurred. It is an event of default under the Forward Purchase Agreements if the State fails to pay when due, or otherwise defaults on, any general obligation bond or any short-term debt, or the validity of any general obligation bond or any short-term debt is contested by the State in a judicial or administrative proceeding. Events of default under the Forward Purchase Agreements also include a judgment that any 2003 Warrants issuable to the Participants is illegal or unenforceable or that any representation or warranty of the State in the Forward Purchase Agreements proved to have been untrue in any material respect when made on June 18, 2003.

If the State draws upon the Forward Purchase Agreements, it will deliver to the Participants registered warrants due immediately and without a maturity date. Repayment by the State of the registered warrants issued to Participants is subordinate in rank of the use of available cash resources on any day to payment of Priority Payments (defined above, which includes the payment of principal and interest on general obligation bonds due on such day) and to rental payments to support lease revenue bonds and principal of and interest on pension obligation bonds due on such day. Daily cash received in excess of the amounts necessary to pay Priority Payments due on such date would be required to be used to repay outstanding registered warrants. The issuance of registered warrants to the Participants will severely restrict the State's cash management flexibility in a manner which could, at least for one or several days, interfere with the State's ability to make Priority Payments on a timely basis. However, the State is confident that it would retain sufficient cash management flexibility to assure the timely payment of debt service on the State's general obligation bonds. See "STATE FINANCES—State Warrants—Registered Warrants" for a description of the nature of registered warrants and the method by which they are repaid, as it relates to other obligations of the State.

The Forward Purchase Agreements contain a number of covenants on the part of the State relating to cash flow management and cash flow borrowing. One covenant requires the State to maximize internal borrowing from special funds prior to borrowing under the Forward Purchase Agreements. See "STATE FINANCES—Inter-Fund Borrowings." Other covenants prohibit the State from issuing any warrants or revenue anticipation notes having a maturity date prior to seven days after the maturity date of the 2003 Warrants.

Fiscal Year 2003-04 Revenue Anticipation Notes

The State issued $3 billion of RANs on October 28, 2003 (the "2003-04 RANs"), which will mature on June 23, 2004. Repayment of principal and interest on $1.835 billion of the 2003-04 RANs is required to be paid from draws under letters of credit (the "Letters of Credit") issued by various financial institutions ("Credit Banks"). The remaining $1.165 billion of 2003-04 RANs ("Unenhanced 2003-04 RANs") were issued directly to various financial institutions (the "Parity Note Purchasers").

As a condition to issuance of the 2003-04 RANs, the Department of Finance estimated that there would be sufficient cash and unused borrowable resources available for use by the General Fund to pay principal of and interest on the 2003-04 RANs when due. Cash flows prepared by the Department of Finance, based upon the 2004-05 Governor's Budget, also estimate that there will be sufficient cash and unused borrowable resources to pay the 2003-04 RANs when due. Such estimate assumed, among other things, receipt by the State of $12.254 billion of economic recovery bond proceeds, which were approved by the voters in March 2004.

If it appears that there will be insufficient available money in the General Fund to pay the principal of and interest on the 2003-04 RANs at maturity, the State has covenanted to use its best efforts to issue registered reimbursement warrants or other obligations, as was done in June 2003, to assure additional cash resources for the General Fund. While no assurance can be given that the State would be able to sell registered reimbursement warrants or other obligations, the State has always been able to borrow funds to meet its cash flow needs in the past and expects to take all steps necessary to continue to have access to the short-term and long-term credit markets. See "STATE FINANCES—State Warrants—Reimbursement Warrants."

If the State is unable to repay the draws upon the Letters of Credit or pay the Unenhanced 2003-04 RANs at maturity, it will deliver registered warrants, due immediately and without a maturity date, to the Credit Banks and the Parity Note Purchasers, as applicable. Repayment by the State of any registered warrants issued to Credit Banks and the Parity Note Purchasers is subordinate in rank to the use of available cash resources on any day to payment of Priority Payments (defined above, which includes the payment of principal and interest on general obligation bonds due on such day), to rental payments to support lease revenue bonds and principal of and interest on pension obligation bonds due on such day and to registered warrants issued to Participants as described above under "2003 Revenue Anticipation Warrants." Daily cash received in excess of the amounts necessary to pay Priority Payments due on such date would be required to be used to repay outstanding registered warrants. The issuance of registered warrants to the Credit Banks and the Parity Note Purchasers will severely restrict the State's cash management flexibility in a manner which could, at least for one or several days, interfere with the State's ability to make Priority Payments on a timely basis. However, the State is confident that it would retain sufficient cash management flexibility to assure the timely payment of debt service on the State's general obligation bonds. See "STATE FINANCES—State Warrants—Registered Warrants" for a description of the nature of registered warrants and the method by which they are repaid, as it relates to other obligations of the State.

STATE FINANCES

The General Fund

The moneys of the State are segregated into the General Fund and over 900 other funds, including special, bond and trust funds. The General Fund consists of revenues received by the State Treasury and not required by law to be credited to any other fund, as well as earnings from the investment of State moneys not allocable to another fund. The General Fund is the principal operating fund for the majority of governmental activities and is the depository of most of the major revenue sources of the State. For additional financial data relating to the General Fund, see the financial statements incorporated in or attached to this APPENDIX A. See "FINANCIAL STATEMENTS." The General Fund may be expended as a consequence of appropriation measures enacted by the Legislature and approved by the Governor (including the annual Budget Act), as well as appropriations pursuant to various constitutional authorizations and initiative statutes.

The Special Fund for Economic Uncertainties

The Special Fund for Economic Uncertainties ("SFEU") is funded with General Fund revenues and was established to protect the State from unforeseen revenue reductions and/or unanticipated expenditure increases. The State Controller may transfer amounts in the SFEU to the General Fund as necessary to meet cash needs of the General Fund and such transfers are characterized as "loans." The State Controller is required to return moneys so transferred without payment of interest as soon as there are sufficient moneys in the General Fund. At the end of each fiscal year, the Controller is required to transfer from the SFEU to the General Fund any amount necessary to eliminate any deficit in the General Fund.

The legislation creating the SFEU (Government Code Section 16418) contains a continuous appropriation from the General Fund authorizing the State Controller to transfer to the SFEU, as of the end of each fiscal year, the lesser of (i) the unencumbered balance in the General Fund and (ii) the difference between the State's "appropriations subject to limitation" for the fiscal year then ended and its "appropriations limit" as defined in Section 8 of Article XIII B of the State Constitution and established in the Budget Act for that fiscal year, as jointly estimated by the State's Legislative Analyst's Office and the Department of Finance. For a further description of Article XIII B, see "State Appropriations Limit." In certain circumstances, moneys in the SFEU may be used in connection with disaster relief.

For budgeting and accounting purposes, any appropriation made from the SFEU is deemed an appropriation from the General Fund. For year-end reporting purposes, the State Controller is required to add the balance in the SFEU to the balance in the General Fund so as to show the total moneys then available for General Fund purposes.

See Table 2 entitled "Internal Borrowable Resources (Cash Basis)" for information concerning the recent balances in the SFEU and projections of the balances for the current and upcoming fiscal years. As in any year, the Budget Act and related trailer bills are not the only pieces of legislation which appropriate funds. Other factors, including re-estimates of revenues and expenditures, existing statutory requirements, existing contractual requirements with respect to the 2003 Warrants and additional legislation introduced and passed by the Legislature may impact the fiscal year-end balance in the SFEU.

Inter-Fund Borrowings

Inter-fund borrowing is used to meet temporary imbalances of receipts and disbursements in the General Fund. In the event the General Fund is or will be exhausted, the State Controller is required to notify the Governor and the Pooled Money Investment Board (the "PMIB," comprised of the State Director of Finance, the State Treasurer and the State Controller). The Governor may then order the State Controller to direct the transfer of all or any part of the moneys not needed in special funds to the General Fund, as determined by the PMIB. All money so transferred must be returned to the special fund from which it was transferred as soon as there is sufficient money in the General Fund to do so. Transfers cannot be made which will interfere with the objective for which such special fund was created, or from certain specific funds. When moneys transferred to the General Fund in any fiscal year from any special fund pursuant to the inter-fund borrowing mechanism exceed ten percent of the total additions to such special fund as shown in the statement of operations of the preceding fiscal year as set forth in the Budgetary (Legal Basis) annual report of the State Controller, interest must be paid on such excess at a rate determined by the PMIB to be the current earning rate of the Pooled Money Investment Account. See also, "CASH FLOW—2003 Revenue Anticipation Warrants" for a description of certain covenants of the State relating to internal borrowings.

As of February 29, 2004, $2.216 billion of outstanding loans from the SFEU and $2.540 billion of outstanding loans from other special funds were used to pay expenditures of the General Fund. See "STATE FINANCES—State Warrants" and "EXHIBIT 1—STATE CONTROLLER'S STATEMENT OF GENERAL FUND CASH RECEIPTS AND DISBURSEMENTS, JULY 1, 2003 THROUGH FEBRUARY 29, 2004 (UNAUDITED)." In addition, as of this date, the State had $10.965 billion of RAWs maturing on June 16, 2004, and $3.0 billion of RANs maturing on June 23, 2004. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Cash Flow Borrowings."

Any determination of whether a proposed borrowing from one of the special funds is permissible must be made with regard to the facts and circumstances existing at the time of the proposed borrowing. The Attorney General of the State has identified certain criteria relevant to such a determination. For instance, amounts in the special funds eligible for inter-fund borrowings are legally available to be transferred to the General Fund if a reasonable estimate of expected General Fund revenues, based upon legislation already enacted, indicates that such transfers can be paid from the General Fund promptly if needed by the special funds or within a short period of time if not needed. In determining whether this requirement has been met, the Attorney General has stated that consideration may be given to the fact that General Fund revenues are projected to exceed expenditures entitled to a higher priority than payment of internal transfers, i.e., expenditures for the support of the public school system and public institutions of higher education and the payment of debt service on general obligation bonds of the State.

At the November 1998 election, voters approved Proposition 2. This proposition requires the General Fund to repay loans made from certain transportation special accounts (such as the State Highway Account) at least once per fiscal year, or up to 30 days after adoption of the annual Budget Act. Since the General Fund may reborrow from the transportation accounts any time after the annual repayment is made, the proposition does not have any adverse impact on the State's cash flow.

In addition to temporary inter-fund borrowings described in this section, budgets enacted in the current and past fiscal years have included other transfers and long-term loans from special funds to the General Fund. In some cases, such loans and transfers have the effect of reducing internal borrowable resources.

The following chart shows internal borrowable resources available for temporary loans to the General Fund on June 30 of each of the fiscal years 2000-01 through 2002-03 and estimates, as of January 9, 2004, for fiscal years 2003-04 and 2004-05. See also "EXHIBIT 1—STATE CONTROLLER'S STATEMENT OF GENERAL FUND CASH RECEIPTS AND DISBURSEMENTS, JULY 1, 2003 THROUGH FEBRUARY 29, 2004 (UNAUDITED)."

TABLE 2
Internal Borrowable Resources
(Cash Basis)
(Millions)

	June 30				
	2001	**2002[(a)]**	**2003[(b)]**	**2004[(c)]**	**2005[(c)]**
Available Internal Borrowable Resources	$12,342.4	$12,979.7	$10,401.5	$11,735.5	$7,172.8
Outstanding Loans					
From Special Fund for Economic Uncertainties	-0-	2,524.5	-0-	2,216.3	634.8
From Special Funds and Accounts	-0-	423.5	-0-	471.5	844.2
Total Outstanding Internal Loans	-0-	2,948.0	-0-	2,687.8	1,479.0
Unused Internal Borrowable Resources	$12,342.4	$10,031.7	$10,401.5	$9,047.7	$5,693.8

(a) At June 30, 2002, the State also had $7.5 billion of outstanding external borrowings in the form of revenue anticipation warrants.

(b) At June 30, 2003, the State also had $10.965 billion of outstanding external borrowings in the form of revenue anticipation warrants.

(c) Department of Finance estimates as of January 9, 2004. Estimates assume the receipt of $12.254 billion of economic recovery bond proceeds prior to June 30, 2004.

Source: State of California, Department of Finance. Information for the fiscal years ended June 30, 2001 through June 30, 2003, are actual figures. Figures for the fiscal years ending June 30, 2004, and June 30, 2005, were estimated as of January 9, 2004, by the Department of Finance.

State Warrants

No money may be drawn from the State Treasury except upon a warrant duly issued by the State Controller. The State Controller is obligated to draw every warrant on the fund out of which it is payable for the payment of money directed by State law to be paid out of the State Treasury; however, a warrant may not be drawn unless authorized by law and unless unexhausted specific appropriations provided by law are available to meet it. State law provides two methods for the State Controller to respond if the General Fund has insufficient "Unapplied Money" available to pay a warrant when it is drawn, referred to generally as "registered warrants" and "reimbursement warrants." "Unapplied Money" consists of money in the General Fund for which outstanding warrants have not already been drawn and which would remain in the General Fund if all outstanding warrants previously drawn and then due were paid subject to the prior application of such money to obligations of the State with a higher priority. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Cash Flow Borrowings." Unapplied Money may include moneys transferred to the General Fund from the SFEU and internal borrowings from State special funds (to the extent permitted by law). See "STATE FINANCES—The Special Fund for Economic Uncertainties" and "—Inter-Fund Borrowings."

Registered Warrants

If a warrant is drawn on the General Fund for an amount in excess of the amount of Unapplied Money in the General Fund, after deducting from such Unapplied Money the amount, as estimated by the State Controller, required by law to be set apart for obligations having priority over obligations to which such warrant is applicable, the warrant must be registered by the State Treasurer on the reverse side as not paid because of the shortage of funds in the General Fund. The State Controller then delivers such a "registered warrant" to persons or entities (e.g., suppliers and local governments) otherwise entitled to receive payments from the State. A registered warrant bears interest at a rate designated by the PMIB up to a maximum of five percent per annum or at a higher rate if issued for an unpaid revenue anticipation note or in connection with some form of credit enhancement such as the Forward Purchase Agreements. See "CASH FLOW—2003 Revenue Anticipation Warrants" for a discussion of the Forward Purchase Agreements. Registered warrants may or may not have a fixed maturity date. Registered warrants that have no fixed maturity date, and registered warrants that bear a maturity date but, for lack of Unapplied Moneys, were not paid at maturity, are paid, together with all interest due, when the Controller, with the approval of the PMIB, determines payment will be made. The State Controller then notifies the State Treasurer, who publishes a notice that the registered warrants in question are payable. The duties of the Controller and the PMIB are ministerial in nature, and the Controller and the PMIB may not legally refuse to pay the principal of or interest on any registered warrants on any date Unapplied Moneys are available in the General Fund after all Priority Payments have been made on that date.

As described under "CASH FLOW—2003 Revenue Anticipation Warrants" and "—Fiscal Year 2003-04 Revenue Anticipation Notes," if the State is required to obtain advances under the Forward Purchase Agreements to pay some or all of the 2003 Warrants (defined above) or draw on the Letters of Credit (defined above) to pay some or all of the 2003-04 RANs at maturity, or is otherwise unable to pay the 2003-04 RANs at maturity, the State will issue registered warrants without a maturity date to the Participants (defined above), Credit Banks (defined above) or Parity Note Purchasers (defined above), as applicable, bringing into effect the daily application of Unapplied Moneys in the General Fund described in the previous paragraph. The adverse results from issuing these registered warrants could include: (1) the State would be required by law to pay the registered warrants before issuing warrants that could be cashed immediately to persons or entities (e.g., suppliers and certain local governments) otherwise entitled to payments from the State General Fund, and the State's ability to manage its cash would therefore be limited; and (2) a default under the State's bank credit facilities backing the State's variable rate general obligation bonds and/or commercial paper notes (which would increase the State's borrowing costs and debt service payments).

Reimbursement Warrants

In lieu of issuing individual registered warrants to numerous creditors, State law provides an alternative procedure whereby the Governor, upon request of the Controller, may authorize utilizing the General Cash Revolving Fund in the State Treasury to borrow from other State special funds to meet payments authorized by law. The Controller may then issue "reimbursement warrants" in the financial market at competitive bid to reimburse the General Cash Revolving Fund, thereby increasing cash resources for the General Fund to cover required payments. The General Cash Revolving Fund exists solely to facilitate the issuance of reimbursement warrants. Reimbursement warrants may have a fixed maturity date.

The principal of and interest on reimbursement warrants must be paid by the Treasurer on their respective maturity dates from any Unapplied Money in the General Fund and available for such payment. In the event that Unapplied Money is not available for payment on the respective maturity dates of reimbursement warrants, and refunding warrants (see "—Refunding Warrants") have not been sold at such times as necessary to pay such reimbursement warrants, such reimbursement warrants will be paid, together with all interest due thereon (including interest accrued at the original interest rate after the maturity date), at such times as the Controller, with the approval of the PMIB, may determine.

The State issued reimbursement warrants on several occasions in order to meet its cash needs during the period 1992-1994, when State revenues were severely reduced because of an economic recession. Facing renewed economic pressures, the State issued reimbursement warrants in June 2002 and in June 2003 (the 2003 Warrants). See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Cash Flow Borrowings," and "CASH FLOW—2003 Revenue Anticipation Warrants."

Refunding Warrants

If there is not sufficient Unapplied Money in the General Fund to pay maturing reimbursement warrants, the Controller is authorized under State law, with the written approval of the Treasurer, to offer and sell a new issue of reimbursement warrants as refunding warrants to refund the prior, maturing reimbursement warrants. Proceeds of such refunding warrants must be used exclusively to repay the maturing warrants. In all other respects, refunding warrants have the same legal status and provisions as reimbursement warrants, as described above.

Sources of Tax Revenue

The following is a summary of the State's major revenue sources. Further information on State revenues is contained under "CURRENT STATE BUDGET" and "STATE FINANCES—Recent Tax Receipts." See Table 4 entitled "Comparative Yield of State Taxes—All Funds, 1999-00 Through 2004-05" for a comparison, by amount received, of the sources of the State's tax revenue.

Personal Income Tax

The California personal income tax, which accounts for a significant portion of General Fund tax revenues, is closely modeled after the federal income tax law. It is imposed on net taxable income (gross income less exclusions and deductions), with rates ranging from 1.0 percent to 9.3 percent. The personal income tax is adjusted annually by the change in the consumer price index to prevent taxpayers from being pushed into higher tax brackets without a real increase in income. Personal, dependent and other credits are allowed against the gross tax liability. In addition, taxpayers may be subject to an alternative minimum tax (AMT), which is much like the federal AMT. The personal income tax structure is considered to be highly progressive. For example, the State Franchise Tax Board indicates that the top 1 percent of taxpayers paid 39.5 percent of the total personal income tax in tax year 2001.

Taxes on capital gains realizations and stock options, which are largely linked to stock market performance, became a larger component of personal income taxes over the last half of the 1990s. The increasing influence that these stock market-related income sources had on personal income tax revenues linked to the highly progressive structure added a significant dimension of volatility to personal income tax receipts. Capital gains and stock option tax receipts peaked in 2000 at $17.6 billion before plunging 51 percent in 2001 to $8.6 billion and dropping an estimated additional 39 percent in 2002 to $5.2 billion. The 2004-05 Governor's Budget forecast assumes moderate growth in capital gains and stock option receipts beginning in 2003-04. See "CURRENT STATE BUDGET—Economic Assumptions."

A proposal included in the 2004-05 Governor's Budget will seek to identify additional taxpayers that do not file tax returns but owe personal income tax. This proposal is estimated to increase revenues by $12 million in fiscal year 2004-05 and $43 million in fiscal year 2005-06.

Sales Tax

The sales tax is imposed upon retailers for the privilege of selling tangible personal property in California. Most retail sales and leases are subject to the tax. However, exemptions have been provided for certain essentials such as food for home consumption, prescription drugs, gas delivered through mains and electricity. Other exemptions provide relief for a variety of sales ranging from custom computer software to aircraft.

The breakdown of the base state and local sales tax rate of 7.25 percent in effect until July 1, 2004, is as follows:

- 5 percent is imposed as a State General Fund tax;
- 0.5 percent is dedicated to local governments for health and welfare program realignment (Local Revenue Fund);
- 0.5 percent is dedicated to local governments for public safety services (Local Public Safety Fund);
- 1.25 percent is a local tax imposed under the Uniform Local Sales and Use Tax Law. Of that amount, 0.25 percent is dedicated to county transportation purposes, and 1 percent is for city and county general-purpose use.

Effective July 1, 2004, the breakdown of the base state and local sales tax rate of 7.25 percent will be as follows:

- 5 percent imposed as a State General Fund tax;
- 0.5 percent dedicated to local governments for health and welfare program realignment (Local Revenue Fund);
- 0.5 percent dedicated to local governments for public safety services (Local Public Safety Fund);
- 1.0 percent local tax imposed under the Uniform Local Sales and Use Tax Law, with 0.25 percent dedicated to county transportation purposes and 0.75 percent for city and county general-purpose use (See "RECENT DEVELOPMENTS REGARDING STATE ECONOMY AND FINANCES" for a discussion of a court action seeking to prohibit the

State Board of Equalization from implementing this one-quarter cent reduction in the local government sales and use tax);

- 0.25 percent deposited into the Fiscal Recovery Fund to repay the State's economic recovery bonds.

Existing law provides that 0.25 percent of the basic 5.00 percent State tax rate may be suspended in any calendar year upon certification by the Director of Finance by November 1 in any year in which both of the following occur: (1) the General Fund reserve (excluding the revenues derived from the 0.25 percent sales and use tax rate) is expected to exceed 3 percent of revenues in that fiscal year (excluding the revenues derived from the 0.25 percent sales and use tax rate) and (2) actual revenues for the period May 1 through September 30 equal or exceed the May Revision forecast. The 0.25 percent rate will be reinstated the following year if the Director of Finance subsequently determines conditions (1) or (2) above are not met for that fiscal year. The reserve was not sufficient to trigger an additional year of reduction for calendar years 2002 through 2004, and the 2004-05 Governor's Budget forecast estimates that the reserve level will again be insufficient to trigger a reduction for calendar year 2005. See "CURRENT STATE BUDGET—Summary of State Revenues and Expenditures" for a projection of the 2004-05 General Fund reserve.

Corporation Tax

Corporation tax revenues are derived from the following taxes:

1. The franchise tax and the corporate income tax are levied at an 8.84 percent rate on profits. The former is imposed on corporations for the privilege of doing business in California, while the latter is imposed on corporations that derive income from California sources but are not sufficiently present to be classified as doing business in the State.

2. Banks and other financial corporations are subject to the franchise tax plus an additional tax at the rate of 2 percent on their net income. This additional tax is in lieu of personal property taxes and business license taxes.

3. The alternative minimum tax (AMT) is similar to that in federal law. In general, the AMT is based on a higher level of net income computed by adding back certain tax preferences. This tax is imposed at a rate of 6.65 percent.

4. A minimum franchise tax of up to $800 is imposed on corporations subject to the franchise tax but not on those subject to the corporate income tax. New corporations are exempted from the minimum franchise tax for the first two years of incorporation.

5. Sub-Chapter S corporations are taxed at 1.5 percent of profits.

Taxpayers with net operating losses (i.e., an excess of allowable deductions over gross income) are allowed to carry forward those losses for tax purposes and deduct a portion in subsequent years. Chapter 488, Statutes of 2002 (AB 2065), suspends the use of any carryover losses for the 2002 and 2003 tax years, but allows taxpayers to deduct those losses beginning in the 2004 tax year and extends the expiration date for those losses by two years. That Chapter also increases the percent of a taxpayer's net operating loss ("NOL") that can be carried forward from 65 percent to 100 percent beginning January 1, 2004, for NOLs generated after that date. About 85 percent of NOL is deducted from corporation taxes with the balance deducted from personal income tax.

On February 23, 2004, the U.S. Supreme Court denied the State Franchise Tax Board's appeal requesting review of the decision in *Farmer Brothers Company v. Franchise Tax Board*, a tax refund case which involved the deductibility of corporate dividends. The exact amount and timing of such refunds is yet to be determined, although potential tax refunds to affected entities could total $400 million over fiscal years 2003-04 through 2007-08. See "LITIGATION—Tax Refund Cases." The reduction in General Fund revenues could result in lower Proposition 98 expenditures, however the potential savings in Proposition 98 expenditures is unknown at this time.

Insurance Tax

The majority of insurance written in California is subject to a 2.35 percent gross premium tax. For insurers, this premium tax takes the place of all other state and local taxes except those on real property and motor vehicles. Exceptions to the 2.35 percent rate are certain pension and profit-sharing plans which are taxed at the lesser rate of 0.5 percent, surplus lines and nonadmitted insurance at 3 percent and ocean marine insurers at 5 percent of underwriting profits.

Estate Tax; Other Taxes

The California estate tax is based on the State death tax credit allowed against the federal estate tax. The California estate tax is designed to pick up the maximum credit allowed against the federal estate tax return. The federal Economic Growth and Tax Reconciliation Act of 2001 phases out the federal estate tax by 2010. As part of this, the Act reduced the State pick-up tax by 25 percent in 2002, 50 percent in 2003, and 75 percent in 2004, and eliminates it beginning in 2005. The provisions of this federal act sunset after 2010. At that time, the federal estate tax will be reinstated along with the State's estate tax, unless future federal legislation is enacted to make the provisions permanent. See Table 4 entitled "Comparative Yield of State Taxes—All Funds, 1999-00 Through 2004-05."

Other General Fund major taxes and licenses include: Inheritance and Gift Taxes; Cigarette Taxes; Alcoholic Beverage Taxes; Horse Racing License Fees and Trailer Coach License Fees.

Special Fund Revenues

The California Constitution and statutes specify the uses of certain revenue. Such receipts are accounted for in various special funds. In general, special fund revenues comprise three categories of income:

- Receipts from tax levies which are allocated to specified functions, such as motor vehicle taxes and fees and certain taxes on tobacco products.
- Charges for special services to specific functions, including such items as business and professional license fees.
- Rental royalties and other receipts designated for particular purposes (e.g., oil and gas royalties).

Motor vehicle related taxes and fees accounted for about 46 percent of all special fund revenues and transfers in 2002-03. Principal sources of this income are motor vehicle fuel taxes, registration and weight fees and vehicle license fees. During fiscal year 2002-03, $7.1 billion was derived from the ownership or operation of motor vehicles. About $5.1 billion of this revenue was returned to local governments. The remainder was available for various State programs related to transportation and services to vehicle owners.

Taxes on Tobacco Products

On November 8, 1988, voters approved Proposition 99, which imposed, as of January 1, 1989, a 25-cent per pack excise tax on cigarettes, and a new, equivalent excise tax on other tobacco products. The initiative requires that funds from this tax be allocated to anti-tobacco education and research, to indigent health services, and environmental and recreation programs.

Proposition 10, which was approved in 1998, increased the excise tax imposed on distributors selling cigarettes in California to 87 cents per pack effective January 1, 1999. At the same time, this proposition imposed a new excise tax on cigars, chewing tobacco, pipe tobacco, and snuff at a rate equivalent to the tax increase on cigarettes. In addition, the higher excise tax on cigarettes automatically triggered an additional increase in the tax on other tobacco products effective July 1, 1999, with the proceeds going to the Cigarette and Tobacco Products Surtax Fund.

The State excise tax on cigarettes of 87 cents per pack and the equivalent rates on other tobacco products are earmarked as follows:

1. Fifty cents of the per-pack tax on cigarettes and the equivalent rate levied on non–cigarette tobacco products are deposited in the California Children and Families First Trust Fund and are allocated primarily for early childhood development programs.

2. Twenty-five cents of the per-pack tax on cigarettes and the equivalent rates levied on non-cigarette tobacco products are allocated to the Cigarette and Tobacco Products Surtax Fund. These funds are appropriated for anti-tobacco education and research, indigent health services, and environmental and recreation programs.

3. Ten cents of the per-pack tax is allocated to the State's General Fund.

4. The remaining two cents of the per-pack tax is deposited into the Breast Cancer Fund.

Chapter 890, Statutes of 2003, imposed a tobacco products licensing requirement which was also designed to reduce overall tobacco tax evasion. Reduced evasion associated with this licensure requirement is expected to generate $36 million ($4 million General Fund) in additional tobacco revenue during the implementation phase in 2003-04 and $70 million ($8 million General Fund) in 2004-05.

Recent Tax Receipts

The following table shows the trend of major General Fund and total taxes per capita and per $100 of personal income for the past four years, the current fiscal year, and the budget year.

TABLE 3
RECENT TAX RECEIPTS

	Trend of State Taxes per Capita[(a)]		Taxes per $100 of Personal Income	
Fiscal Year	**General Fund**	**Total**	**General Fund**	**Total**
1999-00	$2,095.53	$2,447.03	$7.04	$8.22
2000-01	2,222.88	2,589.48	6.87	8.01
2001-02	1,804.21	2,108.96	5.55	6.48
2002-03	1,836.05	2,134.36	5.62	6.53
2003-04[(b)]	1,923.08	2,230.26	5.76	6.68
2004-05[(b)]	2,010.09	2,360.86	5.79	6.80

(a) Data reflect population figures based on the 2000 Census.

(b) Estimated.

Source: State of California, Department of Finance.

The following table gives the actual and estimated revenues by major source for the last four years, the current fiscal year, and the budget year. This table shows taxes, which provide revenue both to the General Fund and State special funds.

TABLE 4
COMPARATIVE YIELD OF STATE TAXES—ALL FUNDS
1999-00 THROUGH 2004-05
(Modified Accrual Basis)
(Thousands of Dollars)

Year Ending June 30	Sales and Use[(a)]	Personal Income	Corporation	Tobacco	Inheritance, Estate and Gift	Insurance	Alcoholic Beverages	Horse Racing	Motor Vehicle Fuel[(b)]	Motor Vehicle Fees[(c)]
2000	$25,525,788	$39,578,237	$6,638,898	$1,216,651	$928,146	$1,299,777	$282,166	$44,130	$3,069,694	$5,263,245
2001	26,616,073	44,618,532	6,899,322	1,150,869	934,709	1,496,556	288,450	42,360	3,142,142	5,286,542
2002	26,004,521	33,051,107	5,333,030	1,102,806	890,627	1,595,846	292,627	42,247	3,295,903	3,836,795
2003	27,177,756	32,713,830	6,803,583	1,055,505	647,372	1,879,784	290,564	40,509	3,202,512	3,965,410
2004[(d)]	26,283,755[(e)]	35,117,000	7,466,000	1,055,100	396,800	1,985,000	292,000	42,245	3,300,369	4,203,880
2005[(d)]	28,974,348[(e)]	38,043,000	7,609,000	1,031,700	135,400	2,078,000	294,000	42,457	3,322,018	4,578,699

(a) Numbers include local tax revenue from the 0.5 percent rate increase dedicated to local governments for the State-local health and welfare program realignment program. The 0.5% rate is equivalent to about $2.3 billion to $2.5 billion per year. The figures also reflect a statutory 0.25 percent reduction which occurred only during calendar year 2001.

(b) Motor vehicle fuel tax (gasoline), use fuel tax (diesel and other fuels), and jet fuel.

(c) Registration and weight fees, motor vehicle license fees and other fees. Vehicle license fee values reflect a 25 percent reduction for 1999 from the 1998 rate of two percent of a vehicle's depreciated value; a 35 percent reduction from such rate for 2000 and the first half of 2001; a 67.5 percent reduction from such rate for the second half of 2001 and thereafter.

(d) Estimated as of January 9, 2004.

(e) The figures do not include voter approved local revenue, the 0.50 percent Local Public Safety Fund revenue, the 1.0 percent local city and county operations revenue (Bradley-Burns), or the 0.25 percent county transportation funds revenue. Estimate for 2004-05 includes $1.256 billion for a temporary one-quarter cent tax increase to be used for repayment of the proposed economic recovery bonds (See "Sources of Tax Revenue—Sales Tax").

NOTE: This table shows taxes which provide revenue both to the General Fund and State special funds. Also, some revenue sources are dedicated to local governments. This accounts for differences between the information in this table and Table 12.

Source: Fiscal years 1999-00 through 2002-03: State of California, Office of the State Controller.
Fiscal years 2003-04 and 2004-05: State of California, Department of Finance.

State Expenditures

The following table summarizes the major categories of State expenditures, including both General Fund and special fund programs.

TABLE 5
GOVERNMENTAL COST FUNDS
(Budgetary Basis)
Schedule of Expenditures by Function and Character
Fiscal Years 1998-99 to 2002-03
(Thousands)

	1998-99	1999-00	2000-01	2001-02	2002-03
Function					
Legislative, Judicial, Executive					
Legislative	$ 219,814	$ 232,323	$ 262,370	$ 265,312	$ 276,462
Judicial[(a)]	1,346,131	1,372,681	1,478,710	1,633,518	2,524,446
Executive	958,189	1,241,219	1,352,128	1,371,891	1,283,297
State and Consumer Services	829,745	856,096	950,192	1,100,942	955,054
Business, Transportation and Housing					
Business and Housing	136,893	156,499	601,053	240,237	184,574
Transportation	4,462,905	5,549,520	4,417,139	6,052,926	3,712,133
Technology, Trade and Commerce	130,796	488,489	140,833	81,832	50,335
Resources	1,695,323	1,858,844	3,349,003	2,284,269	1,993,957
Environmental Protection	600,060	689,678	869,539	993,144	762,052
Health and Human Services	19,616,132	21,806,291	24,204,531	26,563,743	27,420,862
Correctional Programs	4,181,474	4,412,542	4,952,927	5,242,369	5,614,849
Education					
Education–K through 12	22,783,975	26,356,838	28,720,596	28,078,228	27,611,356
Higher Education	7,838,117	8,553,343	9,655,954	9,945,193	9,951,750
Labor and Workforce Development[(b)]	N/A	N/A	N/A	N/A	250,617
General Government					
General Administration	859,703	982,923	1,294,587	2,475,564	1,832,018
Debt Service	1,988,176	2,072,960	2,270,649	2,432,942	2,067,816
Tax Relief	450,213	1,840,129	4,655,826	3,028,703	4,446,940
Shared Revenues	4,151,197	3,677,687	4,385,429	5,528,996	2,784,971
Brown vs. US Dept. of Health and Human Services	–	–	–	96,000	
Other Statewide Expenditures	891,070	580,307	635,475	476,170	525,124
Expenditure Adjustment for Encumbrances[(c)]	(461,310)	(628,506)	(1,943,208)	(681,856)	2,365,727
Credits for Overhead Services by General Fund	(144,041)	(170,594)	(197,343)	(251,575)	(288,871)
Statewide Indirect Cost Recoveries	(32,791)	(37,423)	(36,610)	(47,862)	(50,313)
Total	$72,501,771	$81,891,846	$92,019,780	$96,910,686	$96,275,156
Character					
State Operations	$21,092,849	$22,864,874	$24,850,286	$27,994,343	$26,241,079
Local Assistance	50,734,442	58,369,828	66,087,018	67,993,721	69,043,177
Capital Outlay	674,480	657,144	1,082,476	922,622	990,900
Total	$72,501,771	$81,891,846	$92,019,780	$96,910,686	$96,275,156

(a) Included in this amount are the expenditures of the Trial Court Trust Fund. As of July 1, 2002, the Trial Court Trust Fund was reclassified to a Governmental Cost Fund from a Non-Governmental Cost Fund.

(b) Legislation was enacted effective January 1, 2003 which created a new agency function called the Labor and Workforce Development. The following agencies were transferred from General Government to this new function: the Employment Development Department, the California Workforce Investment Board, the Agricultural Labor Relations Board, and the Department of Industrial Relations.

(c) Expenditures for the State Highway Account (Fund 0042) and the Traffic Congestion Relief Fund (Fund 3007) are reported on a modified cash basis. This method of accounting eliminated all of the continuing appropriations in these two funds.

Source: State of California, Office of the State Controller.

State Appropriations Limit

The State is subject to an annual appropriations limit imposed by Article XIII B of the State Constitution (the "Appropriations Limit"). The Appropriations Limit does not restrict appropriations to pay debt service on voter-authorized bonds.

Article XIII B prohibits the State from spending "appropriations subject to limitation" in excess of the Appropriations Limit. "Appropriations subject to limitation," with respect to the State, are authorizations to spend "proceeds of taxes," which consist of tax revenues, and certain other funds, including proceeds from regulatory licenses, user charges or other fees to the extent that such proceeds exceed "the cost reasonably borne by that entity in providing the regulation, product or service," but "proceeds of taxes" exclude most State subventions to local governments, tax refunds and some benefit payments such as unemployment insurance. No limit is imposed on appropriations of funds which are not "proceeds of taxes," such as reasonable user charges or fees and certain other non-tax funds.

There are various types of appropriations excluded from the Appropriations Limit. For example, debt service costs of bonds existing or authorized by January 1, 1979, or subsequently authorized by the voters, appropriations required to comply with mandates of courts or the federal government, appropriations for qualified capital outlay projects, appropriations for tax refunds, appropriations of revenues derived from any increase in gasoline taxes and motor vehicle weight fees above January 1, 1990 levels, and appropriation of certain special taxes imposed by initiative (e.g., cigarette and tobacco taxes) are all excluded. The Appropriations Limit may also be exceeded in cases of emergency.

The Appropriations Limit in each year is based on the Appropriations Limit for the prior year, adjusted annually for changes in State per capita personal income and changes in population, and adjusted, when applicable, for any transfer of financial responsibility of providing services to or from another unit of government or any transfer of the financial source for the provisions of services from tax proceeds to non-tax proceeds. The measurement of change in population is a blended average of statewide overall population growth, and change in attendance at local school and community college ("K-14") districts. The Appropriations Limit is tested over consecutive two-year periods. Any excess of the aggregate "proceeds of taxes" received over such two-year period above the combined Appropriations Limits for those two years, is divided equally between transfers to K-14 districts and refunds to taxpayers.

The Legislature has enacted legislation to implement Article XIII B which defines certain terms used in Article XIII B and sets forth the methods for determining the Appropriations Limit. California Government Code Section 7912 requires an estimate of the Appropriations Limit to be included in the Governor's Budget, and thereafter to be subject to the budget process and established in the Budget Act.

The following table shows the Appropriations Limit for 2000-01 through 2004-05.

As of the release of the 2004-05 Governor's Budget, the Department of Finance projected the Appropriations Subject to Limit to be $13.449 billion and $12.809 billion under the Appropriations Limit in fiscal years 2003-04 and 2004-05, respectively.

TABLE 6
STATE APPROPRIATIONS LIMIT
(Millions)

	Fiscal Years				
	2000-01	**2001-02**	**2002-03**	**2003-04**	**2004-05**
State Appropriations Limit	$54,073	$59,318	$59,591	$61,702	$63,977*
Appropriations Subject to Limit	(51,648)	(42,240)	(44,462)	(48,253)*	(51,168)*
Amount (Over)/Under Limit	$2,425	$ 17,078	$15,129	$13,449*	$12,809*

* Estimated/Projected.

Source: State of California, Department of Finance.

Proposition 98

On November 8, 1988, voters of the State approved Proposition 98, a combined initiative constitutional amendment and statute called the "Classroom Instructional Improvement and Accountability Act." Proposition 98 changed State funding of public education below the university level and the operation of the State Appropriations Limit, primarily by guaranteeing K-14 schools a minimum share of General Fund revenues. Proposition 98 (as modified by Proposition 111, enacted on June 5, 1990) guarantees K-14 schools the greater of: (a) in general, a fixed percentage of General Fund revenues ("Test 1"), (b) the amount appropriated to K-14 schools in the prior year, adjusted for changes in the cost of living (measured as in Article XIII B by reference to State per capita personal income) and enrollment ("Test 2"), or (c) a third test, which replaces Test 1 and Test 2 in any year the percentage growth in per capita General Fund revenues from the prior year plus one half of one percent is less than the percentage growth in State per capita personal income ("Test 3"). Under Test 3, schools receive the amount appropriated in the prior year adjusted for changes in enrollment and per capita General Fund revenues, plus an additional small adjustment factor. If Test 3 is used in any year, the difference between Test 3 and Test 2 becomes a "credit" (called the "maintenance factor") to schools and the basis of payments in future years when per capita General Fund revenue growth exceeds per capita personal income growth. Proposition 98 implementing legislation adopted prior to the end of the 1988-89 fiscal year determined the K-14 schools' funding guarantee under Test 1 to be 40.3 percent of the General Fund tax revenues, based on 1986-87 appropriations. However, this funding guarantee has been adjusted to approximately 35 percent of 1986-87 appropriations to account for subsequent changes in the allocation of local property taxes, since these changes altered the share of General Fund revenues received by schools. Proposition 98 also contains provisions for the transfer of certain State tax revenues in excess of the Article XIII B limit to K-14 schools in Test 1 years when additional moneys are available. No such transfers are anticipated during 2004-05. See "STATE FINANCES—State Appropriations Limit."

The Proposition 98 guarantee is funded from two sources: local property taxes and the General Fund. Any amount not funded by local property taxes is funded by the General Fund. Thus, local property tax collections represent an offset to General Fund costs in a Test 2 or Test 3 year.

The 2004-05 Governor's Budget reflects General Fund Proposition 98 expenditures in fiscal years 2002-03 through 2004-05 as outlined in the table below. This represents increases in Proposition 98 K-12 spending per pupil of 5.3 and 5.4 percent above the 2002-03 level in 2003-04 and 2004-05, respectively, as well as full funding for statutory growth and COLA. The 2004-05 Governor's Budget also reflects the deferral of Proposition 98 expenditures of $1.897 billion from 2002-03 to 2003-04 and $1.271 billion from 2003-04 to 2004-05 ($200 million for community colleges).

TABLE 7
Proposition 98 Funding
(Dollars in Millions)

	2002-03		2003-04		2004-05	Change From Revised 2003-04	
	Enacted	Revised	Enacted	Revised	Proposed	Amount	Percent
K-12 Proposition 98							
State General Fund	$28,647	$26,106	$27,630	$27,827	$27,233	-$594	-2.1%
Local property tax revenue	12,912	12,800	13,625	13,664	14,709	1,045	7.6%
Subtotals[(a)]	$41,559	$38,906	$41,255	$41,491	$41,942	$451	1.1%
Other Proposition 98							
State General Fund	$2,913	$2,737	$2,353	$2,339	$2,507	$168	7.2%
Local property tax revenue	2,008	1,981	2,105	2,115	2,265	150	7.1%
Subtotals[(a)]	$4,921	$4,718	$4,458	$4,454	$4,772	$318	7.1%
Total Proposition 98							
State General Fund	$31,560	$28,843	$29,983	$30,166	$29,740	-$426	-1.4%
Local property tax revenue	14,920	14,781	15,730	15,779	16,974	1,195	7.6%
Totals[(a)]	$46,480	$43,624	$45,713	$45,945	$46,714	$769	1.7%

(a) Totals may not add due to rounding.

Source: State of California, Department of Finance

Proposition 98 permits the Legislature, by a two-thirds vote of both houses (on a bill separate from the Budget Act), and with the Governor's concurrence, to suspend the K-14 schools' minimum funding guarantee for a one-year period. Restoration of the Proposition 98 funding level to the level that would have been required in the absence of such a suspension occurs over future fiscal years according to a specified State Constitutional formula.

The 2004-05 Governor's Budget proposes that the level of Proposition 98 appropriations be reset at a level approximately $2 billion less than would otherwise be required for 2004-05. If approved, this action would add $2 billion to the existing maintenance factor (defined above) for a total maintenance factor of $4 billion as of the end of fiscal year 2004-05. This cumulative maintenance factor is required to be restored to the Proposition 98 budget in future years as explained above. Assuming a continued moderate economic growth scenario, the Administration projects that $2 billion of the total maintenance factor could be restored in the next three to five fiscal years. The remaining $2 billion maintenance factor would be restored over another three to five fiscal years. Therefore, resetting the minimum funding guarantee as proposed in the 2004-05 Governor's Budget would provide ongoing General Fund savings over several fiscal years until the maintenance factor was fully repaid in approximately 6-10 fiscal years according to current estimates.

Appropriations for 2002-03 and 2003-04 are currently estimated to be $517.8 million and $448.4 million below the amounts required by Proposition 98 because of increases in State tax revenues above original estimates. The Administration proposes to repay these obligations and $250.8 million owed from 1995-96 and 1996-97, over multiple years, beginning in 2006-07.

Local Governments

The primary units of local government in California are the counties, which range in population from 1,200 in Alpine County to approximately 10 million in Los Angeles County. Counties are responsible for the provision of many basic services, including indigent health care, welfare, jails, and public safety in unincorporated areas. There are also 478 incorporated cities and thousands of special districts formed for education, utilities, and other services. The fiscal condition of local governments has been constrained since Proposition 13, which added Article XIII A to the State Constitution, ("Proposition 13") was approved by California voters in 1978. Proposition 13 reduced and limited the future growth of property taxes and limited the ability of local governments to impose "special taxes" (those devoted to a specific purpose) without two-thirds voter approval. Proposition 218, another initiative constitutional amendment enacted in 1996, further limited the ability of local governments to raise taxes, fees, and other exactions. Counties, in particular, have had fewer options to raise revenues than many other local government entities, while they have been required to maintain many services.

In the aftermath of Proposition 13, the State provided aid to local governments from the General Fund to make up some of the loss of property tax moneys, including assuming principal responsibility for funding K-12 schools and community colleges. During the recession of the early 1990s, the Legislature eliminated most of the remaining components of post-Proposition 13 aid to local government entities other than K-12 schools and community colleges by requiring cities and counties to transfer some of their property tax revenues to school districts. However, the Legislature also provided additional funding sources, such as sales taxes, and reduced certain mandates for local services funded by cities and counties. See "STATE FINANCES—Sources of Tax Revenue—Sales Tax" for a discussion of the impact of the proposed bond issuances on local sales taxes. The 2004-05 Governor's Budget proposes to increase transfers to school districts to $1.3 billion, with $135 million coming from community redevelopment agencies and the remainder from cities, counties, and other special districts. In 2003-04, funding is provided for various programs, including the Citizens' Option for Public Safety ("COPS") program to support local front-line law enforcement ($100 million), county juvenile justice and crime prevention programs ($100 million), reimbursement of jail booking fees ($38.2 million), grants to county assessors to increase and enhance property tax assessment activities ($60 million), and open space subvention reimbursements to cities and counties ($39 million). The 2004-05 Governor's Budget proposes to continue funding at these levels for the COPS, county juvenile justice and crime prevention, and property tax assessment grants programs in 2004-05.

Vehicle License Fee

Vehicle license fees are assessed in the amount of two percent of a vehicle's depreciated market value for the privilege of operating a vehicle on California's public highways. A program to offset (or reduce) a portion of the vehicle license fees ("VLF") paid by vehicle owners was established by Chapter 322, Statutes of 1998. Beginning January 1, 1999, a permanent offset of 25 percent of the vehicle license fees paid by vehicle owners became operative. Various pieces of legislation increased the amount of the offset in subsequent years to the existing statutory level of 67.5 percent. This level of offset is expected to provide tax relief of $3.95 billion in fiscal year 2003-04 and $4.06 billion in fiscal year 2004-05.

In connection with the offset of the vehicle license fees, the Legislature authorized appropriations from the State General Fund to "backfill" the offset so that local governments, which receive all of the vehicle license fee revenues, would not experience any loss of revenues. The legislation that established the VLF offset program also provided that if there were insufficient General Fund moneys to fully "backfill" the VLF offset, the percentage offset would be reduced proportionately (i.e., the license fee payable by drivers would be increased) to assure that local governments would not be disadvantaged. In June 2003, the Director of Finance under the Davis Administration ordered the suspension of VLF offsets due to a determination that insufficient General Fund moneys would be available for this purpose, and, beginning in October 2003, vehicle license fees paid by vehicle owners were restored to the 1998 level. However, the offset suspension was rescinded by Governor Schwarzenegger on November 17, 2003, and offset payments to local governments have resumed. Local governments received "backfill" payments totaling $3.80 billion in fiscal year 2002-03. "Backfill" payments totaling $2.65 billion and $4.06 billion are anticipated to be paid to local governments in fiscal years 2003-04 and 2004-05, respectively. Chapter 231, Statutes of 2003, provides for the repayment in August 2006, of approximately $1.3 billion that was not received by locals during the time period between the suspension of the offsets and the implementation of higher fees. See "LITIGATION—Challenges Related to the Vehicle License Fee Offset and Related Payments to Local Governments."

In an unpublished decision issued in September, 2003, the Court of Appeal (*County of San Diego v. Commission on State Mandates et al.*, D039471; petition for review denied by the California Supreme Court, in December, 2003) ruled in favor of the County of San Diego on certain claims related to the medically indigent adult (MIA) program, and determined that the State owed the County of San Diego approximately $3.5 million for medical services rendered to MIAs during the two-year period (1991-1992). See "LITIGATION—Local Government Mandate Claims and Actions." The decision also made the statutory depreciation schedule, which was enacted to fund a portion of the 1991 program realignment between the State and local governments that included MIA programs, inoperative as of March 1, 2004. The Department of Motor Vehicles (DMV) has adopted emergency regulations which establish a replacement depreciation schedule at the prior level. DMV is also proceeding to have these regulations established permanently. If these regulations are established, there will be no change in vehicle license fee revenues available to counties. See "LITIGATION—Local Government Mandate Claims and Actions."

Trial Courts

Prior to legislation enacted in 1997, local governments provided the majority of funding for the State's trial court system. The legislation consolidated the trial court funding at the State level in order to streamline the operation of the courts, provide a dedicated revenue source, and relieve fiscal pressure on the counties. This resulted in decreasing the county contribution for court operations by $415 million and allowed cities to retain $68 million in fine and penalty revenue previously remitted to the State. The State's trial court system will receive approximately $1.8 billion and $1.7 billion in State resources in 2003-04 and 2004-05, respectively, and $475 million in resources from the counties in each fiscal year.

Welfare System

The entire statewide welfare system was changed in response to the change in federal welfare law enacted in 1996 (see "Welfare Reform"). Under the CalWORKs program, counties are given flexibility to develop their own plans, consistent with State law, to implement the program and to administer many of its elements, with costs for administrative and supportive services capped at the 1996-97 levels. As noted above, counties are also given financial incentives if, at the individual county level or statewide, the CalWORKs program produces savings associated with specified standards. Counties are still required to provide "general assistance" aid to certain persons who cannot obtain welfare from other programs.

Welfare Reform

The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (P.L. 104–193, the "Law") fundamentally reformed the nation's welfare system. The Law included provisions to: (i) convert Aid to Families with Dependent Children ("AFDC"), an entitlement program, to Temporary Assistance for Needy Families ("TANF"), a block grant program with lifetime time limits on TANF recipients, work requirements and other changes; (ii) deny certain federal welfare and public benefits to legal noncitizens (subsequent federal law has amended this provision), allow states to elect to deny additional benefits (including TANF) to legal noncitizens, and generally deny almost all benefits to illegal immigrants; and (iii) make changes in the Food Stamp program, including to reduce maximum benefits and impose work requirements. The block grant formula under the Law is operative through June 30, 2004.

Chapter 270, Statutes of 1997, embodies California's response to the federal welfare reforms. Effective January 1, 1998, California Work Opportunity and Responsibility to Kids ("CalWORKs") replaced the former AFDC and Greater Avenues to Independence programs. Consistent with the federal law, CalWORKs contains time limits on the receipt of welfare aid, both lifetime as well as current period. The centerpiece of CalWORKs is the linkage of eligibility to work participation requirements.

Caseload under CalWORKs is continuing to flatten after many consecutive years of decline. The revised CalWORKs caseload projections are 479,000 cases in 2003-04 and 481,000 cases in 2004-05. This represents a major decline in caseload from the rapid growth of the early 1990s, when caseload peaked at 921,000 cases in 1994-95. Since CalWORKs' inception in January 1998, caseload has declined by nearly 35 percent, and the number of working recipients has increased from less than 20 percent in 1996 to nearly 50 percent in 2002.

California will continue to meet, but not exceed, the federally-required $2.7 billion combined State and county maintenance of effort ("MOE") requirement in 2003-04 and 2004-05. In an effort to keep program expenditures within the TANF Block Grant and TANF MOE amounts, the 2004-05 Governor's Budget proposes to eliminate TANF funding for county juvenile probation services, adjust State funding for tribal TANF programs to meet the actual caseloads being served, eliminate the 2004-05 CalWORKs cost-of-living adjustment, and reduce the basic CalWORKs grant.

The 2004-05 Governor's Budget includes an augmentation of $191.9 million in 2003-04 and 2004-05 for employment services to enable recipients to move off of aid and into sustainable employment. The 2004-05 Governor's Budget includes total CalWORKs-related expenditures of $6.9 billion for 2003-04 and $6.4 billion for 2004-05, including child care transfer amounts for the Department of Education and the State's general TANF reserve. The Budget also includes a TANF reserve of $210.1 million, which is available for unanticipated needs in any program for which TANF Block Grant funds are appropriated, including CalWORKs benefits, employment services, county administration, and child care costs. This reserve may be needed for such pressures as litigation or the cost of increased participation rate requirements that have been proposed at the federal level with the reauthorization of the TANF program.

Authorization for the TANF program currently ends June 30, 2004 (having been extended several times from its original September 30, 2002 expiration date). For the TANF program to continue, the U.S. Congress must pass, and the President must sign, legislation reauthorizing the program prior to that date. While Congress and the President will consider several key policy changes, federal reauthorization legislation introduced to date would significantly increase the work participation rate requirements. One proposal would increase work participation rate requirements by 5 percent annually from the current statutory rate of 50 percent to 70 percent in federal fiscal year 2008. The State would need to make substantial investments in child care and employment services in order to meet the increased work participation rate requirements if this proposal was adopted. Failure to meet these increased requirements could result in significant federal penalties.

Pension Trusts

The assets and liabilities of the three principal retirement systems in which the State participates, the California Public Employees' Retirement System ("CalPERS"), the California State Teachers' Retirement System ("CalSTRS") and the University of California Retirement System ("UCRS"), are included in the financial statements of the State as fiduciary funds and described in Note 20 to the Audited Annual Financial Statements of the State of California for the year ended June 30, 2003 (the "Audited Financial Statements"), incorporated by reference in or attached to this APPENDIX A. See "FINANCIAL STATEMENTS."

The three largest defined benefit retirement plans contained in the retirement systems and the excess of the actuarial value of assets over the actuarial accrued liability or unfunded actuarial accrued liability of those plans at June 30, 2002 (June 30, 2001, for CalSTRS) was reported to be as follows:

TABLE 8
ACTUARIAL VALUE OF STATE RETIREMENT SYSTEMS

Name of Plan	Excess of Actuarial Value of Assets Over Actuarial Accrued Liabilities (Unfunded Actuarial Accrued Liability)
Public Employees' Retirement Fund (CalPERS)[1/]	$ (6.653) billion
State Teachers' Retirement Fund Defined Benefit Program (CalSTRS)	(2.227) billion
University of California Retirement Plan	11.549 billion

[1/] Excludes the value of the local government plans of the system.

The actuarial information for CalSTRS for the year ended June 30, 2002, is updated on a two-year cycle and will be available in the spring of 2004. However, according to CalSTRS, its investment portfolio market value as of July 31, 2003, was approximately $100,893,000,000, compared to $92,599,000,000 as of July 31, 2002. The CalPERS reports that its investment portfolio market value as of July 31, 2003, was approximately $145,000,000,000, compared to $135,500,000,000 as of July 31, 2002.

The State's contribution to the CalPERS and the UC Retirement System is actuarially determined each year, while the State's contribution to the CalSTRS is established by statute and is currently 2.017 percent of teacher payroll for the fiscal year ending in the immediately preceding calendar year. The following table shows the State's contributions to CalPERS for fiscal years 1997-98 through 2003-04:

TABLE 9
STATE CONTRIBUTION TO CALPERS
Fiscal Years 1997-98 to 2003-04

1997-98	$1,223,000,000
1998-99	766,100,000
1999-00	463,600,000
2000-01	156,700,000
2001-02	677,200,000
2002-03	1,190,000,000
2003-04	2,213,000,000

Due to past investment losses and increased retirement benefits, the State contribution to CalPERS has increased from $156.7 million in 2000-01 to $2.213 billion in 2003-04. The CalPERS estimates the State's 2004-05 contribution will be approximately $2.564 billion. This estimate will be reevaluated in April 2004, and formal action will be taken by the Board to set the State's 2004-05 retirement contribution in May 2004.

The 2004-05 Governor's Budget proposes a Pension Reform Package to control the State's future costs of pension benefits. The Administration proposes a one-percent increase to existing State employees' annual retirement contributions and will simultaneously pursue legislation to return to the less generous retirement formulae that existed before fiscal year 1999-00 for new State employees. In anticipation of and in order to realize immediate benefits from these reforms, the State plans to issue pension obligation bonds to pay retirement contributions to CalPERS until the effect of returning to pre-2000 benefit levels is sufficiently recognized in CalPERS' actuarial projections. The Administration expects that the litigation concerning the pension obligation bonds will be resolved in sufficient time to allow the State to issue $929 million pension obligation bonds to cover April and June 2005 contributions. It is also estimated that $19.5 million of bonds will be issued in 2005-06. The State would make interest-only payments on the pension obligation bonds in fiscal years 2004-05 through 2007-08 and interest and principal payments in the sixteen fiscal years following. Details concerning the three largest plans and information concerning the other plans contained in the retirement systems are included in Note 20 to the Audited Financial Statements. See "FINANCIAL STATEMENTS."

Repayment of Energy Loans

The Department of Water Resources of the State ("DWR") borrowed $6.1 billion from the General Fund of the State for DWR's power supply program between January and June 2001. DWR issued approximately $11.25 billion in revenue bonds in several series and in the fall of 2002 used the net proceeds of the revenue bonds to repay outstanding loans from banks and commercial lenders in the amount of approximately $3.5 billion and a loan from the General Fund in the amount of $6.1 billion plus accrued interest of approximately $500 million.

The cost of the loans from the General Fund and the banks and commercial lenders that financed DWR's power supply program costs during 2001 exceeded DWR's revenues from the sale of electricity. Since that time, the power supply program has become self-supporting, and no additional loans from the General Fund are authorized. As of January 1, 2003, the DWR's authority to enter into new power purchase contracts terminated, and the three major investor-owned electric utilities (the "IOUs") resumed responsibility for obtaining electricity for their customers.

The general purpose of the power supply program has been to provide to customers of the IOUs the portion of their power not provided by the IOUs. The primary source of money to pay debt service on the DWR revenue bonds is revenues derived from customers of the IOUs resulting from charges set by the California Public Utilities Commission. The DWR revenue bonds are not a debt or liability of the State and do not directly or indirectly or contingently obligate the State to levy or to pledge any form of taxation whatever therefor or to make any appropriation for their payment.

Unemployment Insurance Fund

In fiscal year 2002-03 the State paid $8.161 billion in unemployment benefits from the Unemployment Insurance ("UI") Fund. In fiscal year 2003-04 the State expects to pay $8.203 billion in benefits from the UI Fund. The UI Fund (which is not part of the General Fund) is projected to have a $1.2 billion deficit in calendar year 2004, notwithstanding the automatic unemployment insurance tax rate increase that took effect January 1, 2004. The State may address this issue with one or more of the following options: (1) obtain a loan from the federal government, (2) rollback unemployment benefits and/or (3) increase unemployment insurance taxes which are the sole source of funds for the UI Fund. There is no reason to believe that one or all of these options will not be available to the State. The Employment Development Department (EDD) has applied for a loan from the federal government that would provide cash flow relief so that unemployment benefits can continue to be paid. The federal loan would eventually be repaid from increased UI tax revenue or the available resources resulting from decreased benefits. Interest payments on the loan would be paid by the EDD Contingent Fund and not the General Fund. The Administration and the Legislature will have to determine how to resolve the cash flow imbalance in the UI Fund for the long-term. This issue is expected to be addressed in the upcoming session of the Legislature.

Investment of Funds

Moneys on deposit in the State's Centralized Treasury System are invested by the Treasurer in the Pooled Money Investment Account (the "PMIA"). As of February 29, 2004, the PMIA held approximately $31.3 billion of State moneys, and $22.6 billion invested for about 2,732 local governmental entities through the Local Agency Investment Fund ("LAIF"). The assets of the PMIA as of February 29, 2004, are shown in the following table:

TABLE 10
Analysis of the Pooled Money Investment Account Portfolio*

Type of Security	Amount (Thousands)	Percent of Total
U.S. Treasury	$7,991,984	14.8%
Commercial Paper	10,233,546	19.0
Certificates of Deposits	7,275,039	13.5
Corporate Bonds	1,815,176	3.4
Federal Agency	13,254,846	24.6
Bankers Acceptances	–	0.0
Bank Notes	908,639	1.7
Loans Per Government Code	6,474,215	12.0
Time Deposits	5,844,095	10.8
Repurchases	100,000	0.2
Reverse Repurchases	–	0.0
	$53,897,540	100.0%

* Totals may differ due to rounding.

Source: State of California, Office of the Treasurer.

The State's treasury operations are managed in compliance with the California Government Code and according to a statement of investment policy which sets forth permitted investment vehicles, liquidity parameters and maximum maturity of investments. The PMIA operates with the oversight of the PMIB. The LAIF portion of the PMIA operates with the oversight of the Local Agency Investment Advisory Board (consisting of the State Treasurer and four other appointed members).

The Treasurer does not invest in leveraged products or inverse floating rate securities. The investment policy permits the use of reverse repurchase agreements subject to limits of no more than 10 percent of the PMIA. All reverse repurchase agreements are cash matched either to the maturity of the reinvestment or an adequately positive cash flow date which is approximate to the maturity of the reinvestment.

The average life of the investment portfolio of the PMIA as of February 29, 2004, was 168 days.

THE BUDGET PROCESS

General

The State's fiscal year begins on July 1 and ends on June 30 of the following year. The State operates on a budget basis, using a modified accrual system of accounting for its General Fund, with revenues credited in the period in which they are measurable and available and expenditures debited in the period in which the corresponding liabilities are incurred.

The annual budget is proposed by the Governor by January 10 of each year for the next fiscal year (the "Governor's Budget"). Under State law, the annual proposed Governor's Budget cannot provide for projected expenditures in excess of projected revenues for the ensuing fiscal year. Following the submission of the Governor's Budget, the Legislature takes up the proposal. As required by the Balanced Budget Amendment ("Proposition 58"), beginning with fiscal year 2004-05, the Legislature may not pass a budget bill in which General Fund expenditures exceed estimated General Fund revenues and fund balances at the time of the passage and as set forth in the budget bill.

If the Governor determines that the State is facing substantial revenue shortfalls or spending deficiencies, the Governor is authorized to declare a fiscal emergency. He or she would then be required to propose legislation to address the emergency, and call the Legislature into special session for that purpose. If the Legislature fails to pass and send to the Governor legislation to address the budget fiscal emergency within 45 days, the Legislature would be prohibited from (i) acting on any other bills or (ii) adjourning in joint recess until such legislation is passed. See "THE BUDGET PROCESS – Constraints on the Budget Process" below.

Under the State Constitution, money may be drawn from the Treasury only through an appropriation made by law. The primary source of the annual expenditure appropriations is the annual Budget Act as approved by the Legislature and signed by the Governor. The Budget Act must be approved by a two-thirds majority vote of each House of the Legislature. See "THE BUDGET PROCESS — Constraints on the Budget Process" below. The Governor may reduce or eliminate specific line items in the Budget Act or any other appropriations bill without vetoing the entire bill. Such individual line-item vetoes are subject to override by a two-thirds majority vote of each House of the Legislature.

Appropriations also may be included in legislation other than the Budget Act. Except as noted in the previous paragraph and in the next sentence, bills containing General Fund appropriations must be approved by a two-thirds majority vote in each House of the Legislature and be signed by the Governor. Bills containing appropriations for K-12 schools or community colleges ("K-14 education") only require a simple majority vote. Continuing appropriations, available without regard to fiscal year, may also be provided by statute or the State Constitution.

Funds necessary to meet an appropriation need not be in the State Treasury at the time such appropriation is enacted; revenues may be appropriated in anticipation of their receipt.

Constraints on the Budget Process

Over the years, a number of laws and constitutional amendments have been enacted, often from voter initiatives, which have made it more difficult to raise State taxes, have restricted the use of State General Fund or special fund revenues, or have otherwise limited the Legislature and Governor's discretion in enacting budgets. Prior examples of provisions that make it more difficult to raise taxes include Proposition 13, which, among other provisions, required that any change in State taxes enacted for the purpose of increasing revenues collected pursuant thereto, whether by increased rates or changes in computation, be enacted by a two-thirds vote in each house of the Legislature. Prior examples of provisions restricting the use of General Fund revenue are Proposition 98, which mandates a minimum percentage of General Fund revenues to be spent on local education, and Proposition 10, which raised taxes on tobacco products but mandated how the additional revenues would be expended. See "STATE FINANCES—Proposition 98" and "—Sources of Tax Revenue—Taxes on Tobacco Products."

An initiative statute, Proposition 49, called the "After School Education and Safety Program of 2002," was approved by the voters on November 5, 2002, and will require the State to expand funding for before and after school programs in the State's public elementary and middle schools. In the first year after 2003-04 that non-Proposition 98 appropriations exceed the base year level by $1.5 billion, the initiative will require the State to appropriate up to $550 million annually, depending on the amount of appropriations above the trigger level. The initiative defines the base year level as the fiscal year during the period July 1, 2000, through June 30, 2004, for which the State's non-guaranteed General Fund appropriations are the highest as compared to any other fiscal year during that period. Using data from December 2003, the 2000-01 fiscal year is the base year. Based upon expected non-Proposition 98 General Fund appropriations as of the 2004-05 Governor's Budget, the initiative is unlikely to require implementation of the funding increase for before and after school programs until 2006-07. By comparison, the 2004-05 Governor's Budget includes approximately $121.6 million for these after school programs in both 2003-04 and 2004-05, $428.4 million below the amount which the initiative would require if the full funding increase were in effect.

As noted above, Proposition 58 requires the State to enact a balanced budget, establish a special reserve in the General Fund and restricts future borrowing to cover budget deficits. As a result of the provisions requiring the enactment of a balanced budget and restricting borrowing, the State would, in some cases, have to take more immediate actions to correct budgetary shortfalls. Beginning with the budget for fiscal year 2004-05, Proposition 58 requires the Legislature to pass a balanced budget and provides for mid-year adjustments in the event that the budget falls out of balance.

Proposition 58 also requires that a special reserve (the Budget Stabilization Account) be established in the state's General Fund. Beginning with fiscal year 2006-07, a portion of estimated annual General Fund revenues would be transferred by the Controller into the Budget Stabilization Account no later than September 30 of each fiscal year. These transfers would continue until the balance in the Budget Stabilization Account reaches $8 billion or 5 percent of the estimated General Fund revenues for that fiscal year, whichever is greater. The annual transfer requirement would be in effect whenever the balance falls below the $8 billion or 5 percent target. The annual transfers could be suspended or reduced for a fiscal year by an executive order issued by the Governor no later than June 1 of the preceding fiscal year.

Proposition 58 will also prohibit certain future borrowing to cover budget deficits. This restriction applies to general obligation bonds, revenue bonds, and certain other forms of long-term borrowing. The restriction does not apply to certain other types of borrowing, such as (i) short-term borrowing to cover cash shortfalls in the General Fund (including revenue anticipation notes or revenue anticipation warrants currently used by the State), or (ii) inter-fund borrowings.

Another initiative, Proposition 56, the Budget Accountability Act, which was on the March 2, 2004 ballot and would have reduced from two-thirds to 55 percent the number of votes required to pass the budget bill and other bills related to the budget, including tax increase measures was not approved by the voters.

PRIOR FISCAL YEARS' BUDGETS

Following a severe recession in the early 1990s, the State's financial condition improved markedly starting in 1995-96, due to a combination of better than expected revenues, slowdown in growth of social welfare programs, and continued spending restraint based on actions taken in earlier years. The economy grew strongly between 1994 and 2000, generally outpacing the nation, and as a result, for the five fiscal years from 1995-96 to 1999-00, the General Fund tax revenues exceeded the estimates made at the time the budgets were enacted. These additional funds were largely directed to school spending as mandated by Proposition 98, to make up shortfalls from reduced federal health and welfare aid in 1995-96 and 1996-97 and to fund new program initiatives, including education spending above Proposition 98 minimums, tax reductions, aid to local governments and infrastructure expenditures.

2001 Budget Act

The 2001 Budget Act (for fiscal year 2001-02) was signed by Governor Davis on July 26, 2001. The spending plan for 2001-02 included General Fund expenditures of $78.8 billion, a reduction of $1.3 billion from the prior year. The spending plan utilized more than half of the budget surplus as of June 30, 2001, but still left a projected balance in the SFEU at June 30, 2002, of $2.6 billion. The 2001 Budget Act assumed that, during the course of the fiscal year, the $6.2 billion advanced by the General Fund to the Department of Water Resources for power purchases would be repaid with interest. See "STATE FINANCES—Repayment of Energy Loans."

The final estimate of fiscal year 2001-02 revenues and expenditures, included in the 2003-04 Governor's Budget in January 2003, showed an unprecedented drop in revenues compared to the prior year. The final estimate for the three largest tax sources was $59.7 billion, a drop of over $13 billion from 2000-01, the vast bulk of which was attributable to reduced personal income taxes from stock option and capital gains activity. This revenue shortfall and the delay of the DWR power revenue bonds past June 30, 2002, resulted in a substantial budgetary deficit and cash flow difficulties. Despite a mid-year spending freeze for many State agencies and spending reductions and deferrals totaling $2.3 billion for the 2001-02 fiscal year in January 2002, the State ended fiscal year 2001-02 with a $2.1 billion negative fund balance.

The 2001 Budget Act as initially enacted included Proposition 98 per-pupil spending increases of 4.9 percent. Total General Fund spending of $32.4 billion for K-12 education fully funded enrollment and cost of living increases and also provided additional funding for a number of programs. Higher education funding was increased to allow for enrollment increases at both the University of California and the California State University system with no fee increases. Health and human services generally were fully funded for anticipated caseload growth. Funding for many of these programs was subsequently reduced as a result of the mid-year corrections noted above.

2002 Budget Act

The 2002-03 Governor's Budget, released on January 10, 2002 (the "2002-03 Governor's Budget") projected a combined budget gap for 2001-02 and 2002-03 of approximately $12.5 billion due, in part, to a decline in General Fund revenues attributable to the national economic recession combined with the stock market decline. Personal income tax receipts, which include stock option and capital gains realizations, were particularly affected by the slowing economy and stock market decline. The May Revision to the 2002-03 Governor's Budget projected further deterioration in revenues and additional costs, increasing the two year budget gap to $23.6 billion.

The 2002 Budget Act was signed by Governor Davis on September 5, 2002. The 2002 Budget Act addressed the $23.6 billion gap between expenditures and resources through a combination of program reductions, interfund borrowings, fund shifts, payment deferrals, accelerations and transfers, debt service restructuring savings and modest tax changes.

Within a few months after the 2002 Budget Act was adopted, it became evident that revenue projections incorporated in the 2002 Budget Act were substantially overstated and that certain program cost savings included in the 2002 Budget Act would not be realized.

In late November 2002, Governor Davis directed State agencies to take immediate action to reduce any non-critical or non-essential activities by not filling any vacant positions; to cancel, postpone or amend contracts, grants, purchase orders and similar commitments; to eliminate additional non-essential vacant positions; to delay construction or signing of new leases for space; to cancel or postpone non-essential trips; and to generate new proposals for current year program reductions. In the spring of 2003, the Legislature passed budget adjustment legislation, totaling about $10.4 billion in spending reductions, deferrals and funding transfers ($5.1 billion for 2002-03 and $5.3 billion for 2003-04). The largest part of the reductions (including a $1.1 billion deferral into the 2003-04 fiscal year) were for K-12 education funding.

CURRENT STATE BUDGET

The discussion below of the fiscal year 2003-04 budget and the table under "Summary of State Revenues and Expenditures" are based on estimates and projections of revenues and expenditures for the current fiscal year and future fiscal years and must not be construed as statements of fact. These estimates and projections are based upon various assumptions, which may be affected by numerous factors, including future economic conditions in the State and the nation, and there can be no assurance that the estimates will be achieved. See "RECENT DEVELOPMENTS REGARDING STATE ECONOMY AND FINANCES" and "CURRENT STATE BUDGET—Revenue and Expenditure Assumptions."

Background

The 2003-04 Governor's Budget, released on January 10, 2003 (the "2003-04 Governor's Budget"), projected a significant downward revision in State revenues. The 2003-04 Governor's Budget projected revenues from the three largest tax sources to be about $61.7 billion in 2002-03, more than $6 billion lower than projected in the 2002 Budget Act. The 2003-04 Governor's Budget projected total revenues and transfers of $73.1 billion and $69.2 billion in 2002-03 and 2003-04 respectively. The 2003-04 Governor's Budget projected a $34.6 billion cumulative budget shortfall through June 30, 2004.

The May Revision to the 2003-04 Governor's Budget (the "May Revision") reduced the revenue estimate for 2002-03 to $70.8 billion from the 2003-04 Governor's Budget estimate of $73.1 billion, primarily from the loss of $2 billion of revenues due to the delay of the second sale of tobacco securitization bonds. The May Revision estimated that the cumulative budget shortfall for 2002-03 and 2003-04 had increased from $34.6 billion to $38.2 billion.

2003 Budget Act

After months of negotiation between Governor Davis and the Legislature, the 2003 Budget Act was adopted by the Legislature on July 29, 2003, along with a number of implementing measures, and signed by Governor Davis on August 2, 2003. The 2003 Budget Act largely reflected the proposals contained in the May Revision to the 2003-04 Budget, including, most significantly, the issuance of "fiscal recovery bonds" to address the budget deficit accumulated through June 30, 2003, which was estimated to be $10.675 billion at that time. This estimate has been revised to $8.563 billion, but may be modified further as more financial data is received. Governor Schwarzenegger subsequently proposed, and the voters approved a bond measure on the March 2004 ballot which authorizes the issuance of up to

$15 billion of economic recovery bonds to replace the fiscal recovery bonds. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Economic Recovery Bonds."

Under the 2003 Budget Act, General Fund revenues were projected to increase 3.3 percent, from $70.9 billion in 2002-03 to $73.3 billion in 2003-04. The revenue projections incorporated a 4 percent increase in State tax revenues (as projected by the LAO's office in August of 2003), reflecting a correspondingly moderate growth in the State's economy believed to be reasonable by the State Department of Finance. The projection also incorporated approximately $2 billion of proceeds from the tobacco settlement bonds and $680 million of additional revenue resulting from renegotiating compact agreements between Indian tribes and the State.

General Fund expenditures were estimated to drop 9 percent from $78.1 billion in 2002-03 to $71.1 billion in 2003-04. See "CURRENT STATE BUDGET—2004-05 Governor's Budget" for updated projections regarding fiscal year 2003-04 expenditures. Most of this decline was explained by four factors:

(1) the suspension of vehicle license fee "backfill" payments to local governments, which was estimated to result in $4.2 billion of savings in 2003-04. However, on November 17, 2003, by executive order, Governor Schwarzenegger rescinded the vehicle license fee increase retroactive to October 1 and proposed legislation appropriating $3.625 billion during fiscal year 2003-04 to resume "backfill" payments and to make refund payments to taxpayers. See "LITIGATION—Challenges Related to the Vehicle License Fee Offset and Related Payments to Local Governments;"

(2) approximately $1.8 billion of federal funds under the federal Jobs and Growth Tax Relief Reconciliation Act of 2003 to cover State costs in 2003-04 of which approximately $694 million was to be used to offset Medi-Cal costs in 2003-04, and the remainder was to be used to cover other critical State program spending. These new federal funds are not expected to be available in 2004-05 and beyond;

(3) the receipt of $1.9 billion of pension obligation bond proceeds to cover all of the State's quarterly contributions to CalPERS for 2003-04, which would reduce General Fund expenditures by $900 million and increase revenues by $1 billion. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Pension Obligation Bonds." Delays caused by litigation contesting the issuance of such bonds have made it likely that such bonds will not be issued until fiscal year 2004-05; and

(4) a one-time shift of Medi-Cal accounting from accrual to cash basis ($930 million).

In the LAO's Budget Analysis, dated August 1, 2003, the LAO concluded that, absent the above-described factors, underlying spending for 2002-03 and 2003-04 would be roughly equal. Moreover, the LAO concluded that "the 2003-04 spending level is considerably less than what would be required to maintain "baseline spending" for the [2003-04 fiscal] year." The LAO defines "baseline spending" to include spending requirements imposed by existing law, policies and State mandates at the beginning of the fiscal year.

The June 30, 2004 reserve was projected in the 2003 Budget Act to be just over $2 billion. This projection reflected the elimination of the $10.675 billion accumulated deficit through June 30, 2003 (as estimated in the 2003 Budget Act), through the issuance of the fiscal recovery bonds (which will be replaced by the issuance of economic recovery bonds). See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Economic Recovery Bonds."

Budget Controls and Flexibility

Chapter 228, Statutes of 2003 (AB 1756), authorizes the Director of Finance to reduce appropriations and to reallocate funds among appropriations available to each department in order to ensure the integrity of the 2003 Budget Act. Additionally, the 2003 Budget Act limits the Department of Finance's authority to approve requests for additional funding in the current year ("deficiency requests"). Deficiency requests to fund prior year expenditures, costs associated with legislation enacted without an appropriation, and start-up costs for programs not yet authorized may not be approved.

2004-05 Governor's Budget

The 2004-05 Governor's Budget, released on January 9, 2004, reported that, in the absence of corrective actions to change existing policies, operating deficits, estimated at $14 billion for fiscal 2004-05, would continue to be incurred. The 2004-05 Governor's Budget proposes various corrective actions that result in a balanced budget as described below. The 2004-05 Governor's Budget also revises various revenue and expenditure estimates for 2003-04 and assumes implementation of several mid-year spending reductions as described below.

Fiscal Year 2003-04 Revised Estimates in 2004-05 Governors Budget

In December 2003, the Governor proposed reductions (the "Mid-Year Spending Reduction Proposals") totaling $3.9 billion ($2.3 billion in 2003-04 and $1.6 billion in 2004-05), which are presently being considered by the Legislature. The Mid-Year Spending Reduction Proposals included reductions to Medi-Cal payments and the cancellation of a highway and transit improvement program adopted in calendar year 2000. The 2004-05 Governor's Budget (described below) assumes Legislative approval of these proposals.

The 2004-05 Governor's Budget assumed voter approval in the March 2, 2004 statewide primary election of two measures intended to address these issues: the California Economic Recovery Bond Act (Proposition 57) and the Balanced Budget Amendment (Proposition 58). Both measures were approved by the voters. See "RECENT DEVELOPMENTS REGARDING STATE ECONOMY AND FINANCES." Approval of these measures authorizes the State to issue up to $15 billion in bonds to finance the negative General Fund balance as of June 30, 2004, and other General Fund obligations undertaken prior to June 30, 2004. The State expects to sell a sufficient amount of economic recovery bonds to provide net proceeds to the General Fund in 2003-04 of $12.254 billion. See "RECENT DEVELOPMENTS REGARDING STATE ECONOMY AND FINANCES" and "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Economic Recovery Bonds."

The 2004-05 Governor's Budget projects that the State will end fiscal year 2003-04 with a reserve of $290 million, down approximately $1.9 billion from estimates made at the time of the 2003 Budget Act. Under the 2004-05 Governor's Budget, General Fund revenues for 2003-04 are projected at $77.6 billion, an increase of $4.3 billion compared with 2003 Budget Act estimates. This includes the following significant adjustments since the 2003 Budget Act:

- $2 billion increase in major tax revenues due to the improved economic forecast;
- $3 billion from additional bond proceeds (from the issuance of economic recovery bonds);
- $855 million increase in transfers from transportation funds to the General Fund proposed in the Mid-Year Spending Reduction Proposals;

- $680 million loss in revenues due to delays in renegotiations of tribal gaming compacts;
- $996 million loss in revenues due to present litigation contesting the issuance of pension obligation bonds;
- $120 million increase for other various proposed revenue solutions.

Under the 2004-05 Governor's Budget, General Fund expenditures for 2003-04 were projected at $78.0 billion, an increase of $6.9 billion compared with 2003 Budget Act estimates. This includes the following significant changes since the 2003 Budget Act:

- $885 million in payments of retirement contributions from the General Fund, due to present litigation contesting the issuance of pension obligation bonds;
- $3.0 billion transfer of bond proceeds to the "Deficit Recovery Fund" (from the issuance of economic recovery bonds), a newly created special fund;
- $2.65 billion in expenditures for vehicle license fee offsets due to the rescinding of their suspension (See "STATE FINANCES—Local Governments");
- $183 million (net) additional Proposition 98 expenditures ($631 million due to revenue growth less $448 million for funding below the minimum);
- $660 million additional expenditures due to enrollment and population growth as well as other natural cost increases;
- $155 million for natural disasters (wildfires in Southern California);
- $725 million of savings from various spending reduction proposals, including, among other proposals, additional Medi-Cal provider rate reductions ($161 million), additional reductions pursuant to Control Section 4.10 (which gives the Department of Finance authority to reduce appropriations in certain circumstances) of the 2003 Budget Act ($150 million), and the elimination of the In-Home Supportive Services Residual Program ($88 million). Any potential lost savings (total of $264 million for 2003-04 and $699 million for 2004-05) due to a preliminary injunction preventing the State from implementing Medi-Cal provider rate reductions will be reflected in the May Revision.

Fiscal Year 2004-05 Budget

The 2004-05 Governor's Budget contained the following major components:

1. Resetting Proposition 98 Minimum Funding Guarantee—The level of Proposition 98 appropriations was proposed to be reset at a level approximately $2 billion less than would otherwise be required for 2004-05. This proposal requires a two-thirds vote of the Legislature. See "STATE FINANCES—Proposition 98."

2. Higher Education—The Governor's Budget reflected fee increases of 10 percent for undergraduate and 40 percent for graduate students at the University of California and the California State University, of which 20 percent will be set aside for financial aid. (In fiscal year 2003-04, such fees were increased 30 percent.) The Governor's Budget also reflected fees of $26 per unit for community college undergraduates and $50 per unit for degree holders, up from $18 in 2003-04.

3. Health and Human Services—The Administration proposed major reform of the Medi-Cal program in the Governor's Budget. Key components included realigning eligibility standards, requiring copayments, implementing a tiered benefit structure, and conforming basic optional benefits to those offered under private plans. The Administration also proposed to increase work incentives under the CalWORKs program as well as reductions to the services and assistance payments provided under that program.

4. Tax Relief—Full reimbursement to local governments for the vehicle license fee offsets program is proposed. See "STATE FINANCES—Local Governments."

5. Pension Reform—The Governor's Budget proposed to increase existing State employees' retirement contributions by one percent, pursue legislation to repeal retirement benefit enhancements implemented in 1999 for new State employees, and issue pension obligation bonds to cover a portion of the pension contributions in 2004-05 and 2005-06.

6. California Performance Review—The Administration revealed its plan to conduct a fundamental review of State government that would focus on the following areas: executive branch reorganization, program performance assessment and budgeting, improved services and productivity, and acquisition reform.

7. Substantially Reduced External Borrowings—The Administration proposes to issue $929 million pension obligation bonds to pay a portion of the pension obligations in 2004-05. In addition, approximately $3 billion of economic recovery bond proceeds deposited in the Deficit Recovery Fund will be used to offset fiscal year 2004-05 expenditures. In contrast, in fiscal year 2003-04, aggregate borrowings to address current expenses and accumulated deficits are estimated at $11.5 billion, including $2.3 billion of tobacco securitization proceeds and the projected $9.2 billion of economic recovery proceeds (representing $12.3 billion of total bond proceeds, less $3 billion deposited into the Deficit Recovery Fund).

The 2004-05 Governor's Budget projected to end fiscal year 2004-05 with a $635 million reserve. General Fund revenues for 2004-05 were projected at $76.4 billion, a decrease of $1.2 billion compared with revised estimates for 2003-04. This budget reflects the following major items and changes from fiscal year 2003-04:

- $4.2 billion (or six percent) increase in major revenues due to the improved economic forecast;
- $577 million of transfers to the General Fund, resulting from the issuance of pension obligation bonds in fiscal year 2004-05 to cover a portion of the pension contributions;
- $500 million additional revenues as a result of the renegotiation of tribal gaming compacts and the negotiation of new compacts with tribes that wish to expand gaming activities;
- $300 million additional revenues from proposed fees on Medi-Cal managed care plans;
- $855 million decrease for transportation transfers (one-time transfer in 2003-04);
- $650 million decrease for one-time transfers and loans in 2003-04.

General Fund expenditures for 2004-05 were projected at $76.1 billion, a decrease of $2.0 billion compared with revised estimates for 2003-04. This reflects a total of $13.3 billion of General Fund expenditure solutions, spending reductions from the level of expenditures that would have been required to comply with the Constitution and State law, federal government mandates, court orders, and to provide for cost of living adjustments and growth in enrollment, caseload, and population. These expenditure solutions, include, among others, the following major items and changes from fiscal year 2003-04:

- $3.012 billion of General Fund payment offsets from economic recovery bond proceeds deposited in the Deficit Recovery Fund;

- $2.004 billion for the proposal to rebase the Proposition 98 guarantee (see "STATE FINANCES—Proposition 98");

- $1.336 billion for funding Proposition 98 expenditures with local property taxes that previously were funded with General Fund;

- $1.256 billion for debt service savings reflecting the anticipated lower cost of economic recovery bonds compared with debt service on fiscal recovery bonds;

- $1.127 billion for the proposed suspension of the Transportation Investment Fund transfer;

- $352 million from the proposed issuance of pension obligation bonds in fiscal year 2004-05 to cover a portion of the pension contributions;

- $350 million for additional federal funds anticipated to be received in 2004-05;

- $462 million for proposed Medi-Cal provider rate reductions. Any potential lost saving due to a preliminary injunction preventing the State from implementing Medi-Cal provider rate reductions will be reflected in the May Revision;

- $1.524 billion for various spending reductions in social services programs;

- $400 million for spending reductions that would result from changes in the correctional system. This proposal is still in the process of being developed and will be submitted to the Legislature in May;

- $150 million for additional savings pursuant to Control Section 4.10 (which gives the Department of Finance authority to reduce appropriations in certain circumstances) of the 2003 Budget Act;

- $729 million for various spending reductions in higher education.

Continuing "Structural Deficit"

In its November 2003 "Fiscal Recovery" Report, the Legislative Analyst's Office ("LAO") concluded: "the State faces a major mismatch between revenues and expenditures, and this will ultimately need to be addressed through spending reductions and/or revenue enhancements if the State is to regain fiscal balance."

In its February 18, 2004 analysis of the 2004-05 Governor's Budget the LAO states: "[T]he Governor's proposal [i.e., the 2004-05 Governor's Budget] is a solid starting point for budgetary negotiations." However, the LAO cautions that some of the solutions (including savings realized from the issuance of pension obligation bonds, Medi-Cal rate reduction and the renegotiation of tribal gaming compacts) in the Governor's proposal may not be realized and could increase the budget shortfall for 2004-05 to about $4 billion. The LAO adds that a "$7 billion ongoing gap between revenues and expenditures would occur in 2005-06 and continue in subsequent years, absent further corrective action." The LAO concludes that additional savings proposals or revenue increases will be necessary to resolve the state's "budget shortfall."

The Administration expects that any shortfall in 2005-06 would be lower than projected by the LAO due to savings that are expected to be achieved in 2005-06 and thereafter from proposals to reform Medi-Cal, In-Home Supportive Services, CalWORKs, corrections and pension contributions.

Summary of State Revenues and Expenditures

The table below presents the actual revenues, expenditures and changes in fund balance for the General Fund for fiscal years 2000-01, 2001-02, and 2002-03, estimated results for fiscal year 2003-04 and projected results (based upon the 2004-05 Governor's Budget) for fiscal year 2004-05.

TABLE 11
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE–GENERAL FUND
(Budgetary Basis)[a]
FISCAL YEARS 2000-01 THROUGH 2004-05
(Millions)

	2000-01	2001-02	2002-03	Estimated[b] 2003-04[c]	Proposed[b] 2004-05[c]
Fund Balance–Beginning of Period	$ 9,639.7	$ 9,017.5	$ (2,109.8)	$ (7,536.2)	$ 1,218.6
Restatements					
Economic Recovery Bonds[d]	–	–	–	9,242.0	–
Prior Year Revenue, Transfer Accrual Adjustments	(158.8)	(729.8)	154.4	3.5	–
Prior Year Expenditure, Accrual Adjustments	(229.9)	217.4	374.2	(102.0)	–
Fund Balance–Beginning of Period, as Restated	$ 9,251.0	$ 8,505.1	$ (1,581.2)	$1,607.3	$ 1,218.6
Revenues	$77,609.9	$ 64,060.3	$68,545.8	$73,107.9	$75,609.3
Other Financing Sources					
Economic Recovery Bonds[d]	–	–	–	3,012.0	–
Transfers from Other Funds	6,561.8[e]	2,143.3	3,289.5	1,519.5	797.4
Other Additions	46.3	33.9	143.9	–	–
Total Revenues and Other Sources	$84,218.0	$ 66,237.5	$71,979.2	77,639.4	$76,406.7
Expenditures					
State Operations	$17,641.7	$ 19,085.7	$18,277.6	$16,946.3	$18,463.2
Local Assistance	58,441.4	57,142.0	59,145.3	57,659.7	60,927.9
Capital Outlay	2,044.3	323.5	141.3	410.1	32.8
Unclassified	–	–	–	3,012.0[f]	(3,362.0)[g]
Other Uses					
Transfer to Other Funds	6,324.1[e]	301.2	370.0	–[h]	–[h]
Total Expenditures and Other Uses	$84,451.5	$ 76,852.4	$ 77,934.2	$78,028.1	$ 76,061.9
Revenues and Other Sources Over or (Under) Expenditures and Other Uses	$ (233.5)	$(10,614.9)	$ (5,955.0)	$ (388.7)	$ 344.8
Fund Balance					
Reserved for Encumbrances	$ 1,834.3	$ 1,491.5	$ 1,037.4	$ 928.7	$ 928.7
Reserved for Unencumbered Balances of Continuing Appropriations[i]	1,436.7	827.3	996.9	471.3	155.9
Reserved for School Loans[j]	349.7	–	–	–	–
Unreserved–Undesignated [k]	5,396.8	(4,428.6)	(9,570.5)	(181.4)	478.8
Fund Balance–End of Period	$ 9,017.5	$ (2,109.8)	$ (7,536.2)	$1,218.6	$ 1,563.4

Footnotes on following page.

Source: Fiscal years 2000-01 to 2002-03: State of California, Office of the State Controller.
Fiscal years 2003-04 and 2004-05: State of California, Department of Finance.

(a) These statements have been prepared on a budgetary basis in accordance with State law and some modifications would be necessary in order to comply with generally accepted accounting principles ("GAAP"). The Supplementary Information contained in the State's Audited Annual Financial Statements for the year ended June 30, 2003, incorporated by reference in this APPENDIX A, contains a description of the differences between the budgetary basis and the GAAP basis of accounting and a reconciliation of the June 30, 2002 fund balance between the two methods.

(b) Estimates are shown net of reimbursements and abatements.

(c) Estimated as of the 2004-05 Governor's Budget, January 9, 2004.

(d) Reflects the Administration's proposal to finance the negative General Fund reserve balance as of June 30, 2004, and other General Fund obligations undertaken prior to June 30, 2004, through the issuance of economic recovery bonds sufficient to provide net proceeds to the General Fund of $12.254 billion in 2003-04. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Economic Recovery Bonds." For budgeting purposes, $9.242 billion of this amount is shown in 2002-03 to reflect that the accumulated deficit has been eliminated as of the start of fiscal year 2003-04.

(e) "Transfers to Other Funds" includes the $6.2 billion General Fund loan to the Department of Water Resources Electric Power Purchase Fund. See "STATE FINANCES—Repayment of Energy Loans" and "CURRENT STATE BUDGET" in this APPENDIX A. "Transfers from Other Funds" includes this loan as a receivable in 2000-01. The loan was subsequently repaid with interest as follows: $116 million in July 2001, $164 million in October 2002, and $6.456 billion in November 2002. The loan was reported in the State's Budgetary/Legal Basis Annual Report as an asset of the General Fund and a liability of the Department of Water Resources Electric Power Purchase Fund.

(f) Reflects the transfer of $3.012 billion economic recovery bond proceeds from the General Fund to the Deficit Recovery Fund.

(g) Reflects General Fund payment offsets from moneys deposited in the Deficit Recovery Fund ($3.012 billion) and from new federal funds ($350 million).

(h) "Transfer to Other Funds" is included either in the expenditure totals detailed above or as "Transfer from Other Funds."

(i) For purposes of determining whether the General Fund budget, in any given fiscal year, is in a surplus or deficit condition, Chapter 1238, Statutes of 1990, amended Government Code Section 13307. As part of the amendment, the unencumbered balances of continuing appropriations which exist when no commitment for an expenditure is made should be an item of disclosure, but the amount shall not be deducted from the fund balance. Accordingly, the General Fund condition included in the 2004-05 Governor's Budget includes the unencumbered balances of continuing appropriations as a footnote to the statement ($587.4 million in 2002-03, $471.3 million in 2003-04 and $155.9 million in 2004-05). However, in accordance with Government Code Section 12460, the State's Budgetary/Legal Basis Annual Report reflects a specific reserve for the encumbered balance for continuing appropriations.

(j) During 1995, a reserve was established in the General Fund balance for the $1.7 billion of previously recorded school loans which had been authorized by Chapter 703, Statutes of 1992 and Chapter 66, Statutes of 1993. These loans were repaid from future General Fund appropriations as part of the settlement of litigation. This accounting treatment is consistent with the State's audited financial statements prepared in accordance with GAAP.

(k) Includes Special Fund for Economic Uncertainties (SFEU). The Department of Finance generally includes in its estimates of the SFEU and set aside reserves, if any, the items reported in the table under "Reserved for Unencumbered Balances of Continuing Appropriations," "Reserved for School Loans," and "Unreserved—Undesignated." The Department of Finance projects a $289.9 million SFEU balance on June 30, 2004, and a $634.8 million SFEU balance on June 30, 2005, based upon the 2004-05 Governor's Budget released on January 9, 2004.

Revenue and Expenditure Assumptions

The table below presents the Department of Finance's budget basis statements of major General Fund revenue sources and expenditures for the 2002-03 fiscal year and 2004-05 Governor's Budget estimates for the 2003-04 and 2004-05 fiscal years.

TABLE 12
Major General Fund Revenue Sources and Expenditures

	Revenues (Millions)			
	Fiscal Years			
Source	**2002-03[a] Actual**	**2003-04[b] Enacted**	**2003-04[c] Revised**	**2004-05[c] Proposed**
Personal Income Tax	$32,710	$33,596	$35,117	$38,043
Sales and Use Tax	22,415	23,518	23,714	25,022
Corporation Tax	6,804	7,035	7,466	7,609
Insurance Tax	1,880	2,068	1,985	2,078
Economic Recovery Bonds[d]	9,242	–	3,012	–
All Other	7,513[e]	7,136[f]	6,345[g]	3,655[h]
Total Revenues and Transfers	$80,564	$73,353	$77,639	$76,407

	Expenditures (Millions)			
	Fiscal Years			
Function	**2002-03[a] Actual**	**2003-04[b] Enacted**	**2003-04[c] Revised**	**2004-05[c] Proposed**
K-12 Education	$28,788	$29,318	$29,558	$30,317
Health and Human Services	23,060	23,358	22,789	24,600
Higher Education	9,488	8,679	8,722	8,694
Youth and Adult Correctional	5,837	5,644	5,326	5,732
Legislative, Judicial and Executive	2,459	2,406	2,528	2,616
Tax Relief	4,447	707[i]	3,365	4,730
Resources	1,147	865	985	939
State and Consumer Services	468	444	471	478
Business, Transportation and Housing	206	512	518	375
All Other	1,582	-796[j]	3,766[k]	-2,419[l]
Total Expenditures	$76,482	$71,137	$78,028	$76,062

Footnotes continue on following page.

Source: State of California, Department of Finance. Figures in this table may differ from the figures in Table 4; see "Note" to Table 4.

(a) Figures for 2002-03, prepared by the Department of Finance, are slightly different than the figures in Table 11, prepared by the State Controller's Office, because of certain differences in accounting methods used by the two offices.

(b) 2003 Budget Act, August 2, 2003.

(c) 2004-05 Governor's Budget, January 9, 2004.

(d) Reflects the Administration's proposal to finance the cumulative deficit over several years through the issuance of economic recovery bonds sufficient to provide $12.254 billion net proceeds to the General Fund in 2003-04. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS— Economic Recovery Bonds."

(e) Includes $2.5 billion for tobacco securitization bond proceeds and about $2.8 billion in inter-fund loans and transfers.

(f) Includes $2.0 billion for tobacco securitization bond proceeds. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Enhanced Tobacco Settlement Revenue Bonds." Also includes the anticipated receipt of $996 million from pension obligation bonds, which would be used to offset special fund contributions to pension funds. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Pension Obligation Bonds."

(g) Includes $2.264 billion for tobacco securitization bond proceeds and about $1.5 billion in inter-fund loans and transfers. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Enhanced Tobacco Settlement Revenue Bonds."

(h) Includes $500 million for Indian gaming revenues and about $800 million in inter-fund loans and transfers.

(i) Reflects the suspension of vehicle license fee "backfill" payments to local governments, which was rescinded on November 17, 2003. See "STATE FINANCES—Local Governments."

(j) Reflects reduced expenditures of $912 million due to the anticipated receipt of pension obligation bond proceeds to cover General Fund contributions to pension funds. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS—Pension Obligation Bonds."

(k) Reflects the transfer of $3.012 billion of economic recovery bond proceeds to the Deficit Recovery Fund.

(l) Reflects $3.012 billion of General Fund payments to be offset with moneys deposited in the Deficit Recovery Fund.

Development of Revenue Estimates

The development of the forecast for the major General Fund revenues begins with a forecast of national economic activity prepared by an independent economic forecasting firm. The Department of Finance's Economic Research Unit, under the direction of the Chief Economist, adjusts the national forecast based on the Department's economic outlook. The national economic forecast is used to develop a forecast of similar indicators for California activity.

After finalizing the forecasts of major national and California economic indicators, revenue estimates are generated using revenue forecasting models developed and maintained by the Department of Finance. With each forecast, adjustments are made for any legislative, judicial, or administrative changes, as well as for recent cash results. The forecast is updated twice a year and released with the Governor's Budget by January 10 and the May Revision by May 14.

Economic Assumptions

The revenue and expenditure assumptions set forth above have been based upon certain estimates of the performance of the California and national economies in calendar years 2004 and 2005. In the 2004-05 Governor's Budget, the Department of Finance projected that the California economy would grow moderately in calendar year 2004 and at a faster pace in calendar year 2005.

Both the California economy and the national economy have been sluggish in the last calendar year. From December 2002 to December 2003, nonfarm payroll employment fell by 0.2 percent in the State and 0.1 percent in the nation. The state unemployment rate was 6.4 percent in December, down from 6.9 percent a year earlier. Similarly, the national unemployment rate in December 2003 was 5.7 percent, down from 6.0 percent a year earlier. On the other hand, both homebuilding and housing markets were strong in both the State and the nation in 2003.

While California labor markets did not show signs of improvement in 2003, broader economic measures did. Total personal income increased for the sixth consecutive quarter in the second quarter of 2003. Exports of made-in-California merchandise began to increase again in the third quarter of 2003 after falling for nearly three years. Taxable sales posted a fifth consecutive year-over-year gain in the third quarter of 2003. Two regional manufacturing surveys showed improvement comparable to that seen in the second half of 2003 for the nation's manufacturing sector. Personal state income tax withholdings were up 5.9 percent in 2003, at least partly due to increased employee stock option income.

In addition, construction and real estate markets remained strong in the state in 2003. Permits for 178,900 new residential units were issued in the first 11 months, up 15 percent from the year-ago level.

For 2003 as a whole, residential construction will be higher than it has been since 1989. Private nonresidential building continued to decline marginally, however.

Home prices continued to rise in 2003. The median price of existing, single-family houses sold in California was up between 14 and 16 percent, with the median price over $400,000 for the first time in August. Sales also increased slightly—between 4 and 6 percent. According to the California Association of Realtors, only one in four California households would have been able to afford a median-priced home in November of 2003.

As noted above, the 2004-05 Governor's Budget projects moderate growth in calendar year 2004 and faster growth in calendar year 2005. Unemployment is expected to remain above 6 percent throughout the period. Personal income is projected to grow 5.6 percent in 2004 and 5.9 percent in 2005, which is slower than has been observed in past recoveries. While low interest rates and federal fiscal stimulus are expected to boost the state economy in 2004, expenditure reductions will have the opposite effect.

The Department of Finance set out the following estimates for the State's economic performance in calendar years 2004 and 2005, which were used in predicting revenues and expenditures for the 2004-05 Governor's Budget. Also shown is the Department of Finance's previous forecast for the same calendar years, contained in the May Revision to the 2003-04 Governor's Budget.

TABLE 13
ESTIMATES OF STATE'S ECONOMIC PERFORMANCE

	For Calendar Year 2004		For Calendar Year 2005	
	2003-04 May Revision[(a)]	2004-05 Governor's Budget[(b)]	2003-04 May Revision[(a)]	2004-05 Governor's Budget[(b)]
Non-farm wage and salary employment (000)	14,922	14,602	15,282	14,906
Percent Change	2.1%	1.1%	2.4%	2.1%
Personal income ($ billions)	$1,232	$1,266	$1,302	$1,341
Percent Change	4.9%	5.6%	5.7%	5.9%
Housing Permits (Units 000)	174	192	189	198
Consumer Price Index (percent change)	2.4%	1.9%	2.8%	2.7%

(a) Fiscal Year 2003-04 May Revision to the Governor's Budget: May 14, 2003.

(b) Fiscal Year 2004-05 Governor's Budget Summary: January 9, 2004.

Source: State of California, Department of Finance.

FINANCIAL STATEMENTS

The Audited Annual Financial Statements of the State of California for the Year Ended June 30, 2003 (the "Financial Statements") are available. As of June 30, 2002, the State of California has implemented a new financial reporting model, as required by the Governmental Accounting Standards Board ("GASB") in conformity with accounting principles generally accepted in the United States of America. The GASB sets standards of accounting and financial reporting for state and local governments, which have significantly changed the presentation of the financial statements. The Financial Statements consists of an Independent Auditor's Report, a Management Discussion and Analysis, Basic Financial Statements of the State for the Year Ended June 30, 2003 ("Basic Financial

Statements"), and Supplementary Information. Only the Basic Financial Statements have been audited, as described in the Independent Auditor's Report. A description of the new accounting and financial reporting standards is contained in Note 1 of the Basic Financial Statements.

Potential investors may obtain or review a copy of the Financial Statements from the following sources:

1. By obtaining from any Nationally Recognized Municipal Securities Information Repository, or any other source, a copy of the State of California's Official Statement dated March 24, 2004, relating to the issuance of $186,110,000 State Public Works Board Lease Revenue Refunding Bonds (Department of Corrections), Series D and $93,975,000 of State Public Works Board Lease Revenue Refunding Bonds (Department of Corrections), Series E. The Financial Statements are printed in full in such Official Statement. No part of the March 24, 2004 Official Statement is incorporated into this document except the Financial Statements.

2. By accessing the internet website of the State Controller (www.sco.ca.gov) and selecting "California Government—State and Local," then "State Government," then finding the heading "Publications" and selecting "Comprehensive Annual Financial Report—Year Ended June 30, 2003," or by contacting the Office of the State Controller at (916) 445-2636.

3. By accessing the internet website of the State Treasurer (www.treasurer.ca.gov) and selecting "Financial Information" and then "Audited General Purpose Financial Statements," or by contacting the Office of the State Treasurer at (800) 900-3873.

The State Controller's unaudited reports of cash receipts and disbursements for the period July 1, 2003 through February 29, 2004 is also included as an Exhibit to this APPENDIX A and is available on the State Controller's website.

Periodic reports on revenues and/or expenditures during the fiscal year are issued by the Administration, the State Controller's Office and the Legislative Analyst's Office. The State Controller issues a monthly report on cash receipts and disbursements recorded on the Controller's records. The Department of Finance issues a monthly bulletin, available by accessing the internet website of the Department of Finance (www.dof.ca.gov), which reports the most recent revenue receipts as reported by State departments, comparing those receipts to budget projections. The Administration also formally updates its budget projections three times during each fiscal year, in January, May, and at the time of budget enactment. These bulletins and reports are available on the internet at websites maintained by the agencies and by contacting the agencies at their offices in Sacramento, California. Such bulletins and reports are not part of or incorporated into the Official Statement. Investors are cautioned that interim financial information is not necessarily indicative of results for a fiscal year. Information which may appear in the Official Statement from the Department of Finance concerning monthly receipts of "agency cash" may differ from the State Controller's reports of cash receipts for the same periods because of timing differences in the recording of in-transit items.

OVERVIEW OF STATE GOVERNMENT

Organization of State Government

The State Constitution provides for three separate branches of government: the legislative, the judicial and the executive. The Constitution guarantees the electorate the right to make basic decisions, including amending the Constitution and local government charters. In addition, the State voters may directly influence State government through the initiative, referendum and recall processes.

California's Legislature consists of a forty-member Senate and an eighty-member Assembly. Assembly members are elected for two-year terms, and Senators are elected for four-year terms. Assembly members are limited to three terms in office and Senators to two terms. The Legislature meets almost year round for a two-year session. The Legislature employs the Legislative Analyst, who provides reports on State finances, among other subjects. The Bureau of State Audits, headed by the State Auditor, an independent office since 1993, annually issues an auditor's report based on an examination of the General Purpose Financial Statements of the State Controller, in accordance with generally accepted accounting principles. See "FINANCIAL STATEMENTS."

The Governor is the chief executive officer of the State and is elected for a four-year term. The Governor presents the annual budget and traditionally presents an annual package of bills constituting a legislative program. In addition to the Governor, State law provides for seven other statewide elected officials in the executive branch. The current elected statewide officials, their party affiliation and the dates on which they were first elected are as follows:

Office	**Name**	**Party Affiliation**	**First Elected**
Governor	Arnold Schwarzenegger	Republican	2003
Lieutenant Governor	Cruz Bustamante	Democrat	1998
Controller	Steve Westly	Democrat	2002
Treasurer	Philip Angelides	Democrat	1998
Attorney General	Bill Lockyer	Democrat	1998
Secretary of State	Kevin Shelley	Democrat	2002
Superintendent of Public Instruction	Jack O'Connell	Democrat	2002
Insurance Commissioner	John Garamendi	Democrat	2002

The current term for each office expires in January 2007. Persons elected to statewide offices are limited to two terms in office (eight years) from the dates shown above. Mr. Garamendi previously served as elected Insurance Commissioner before term limits were enacted. Governor Schwarzenegger may seek re-election in 2006 to one term.

The executive branch is principally administered through eleven major agencies and departments: Business, Transportation and Housing Agency, Child Development and Education Agency, Environmental Protection Agency, Department of Finance, Department of Food and Agriculture, Health and Human Services Agency, Labor and Workforce Development Agency, Resources Agency, State and Consumer Services Agency, Department of Veterans Affairs and Youth and Adult Correctional Agency. In addition, some State programs are administered by boards and commissions, such as The Regents of the University of California, Public Utilities Commission, Franchise Tax Board and California Transportation Commission, which have authority over certain functions of State government with the power to establish policy and promulgate regulations. The appointment of members of boards and commissions is usually shared by the Legislature and the Governor, and often includes ex officio members.

California has a comprehensive system of public higher education comprised of three segments: the University of California, the California State University System and California Community Colleges. The University of California provides undergraduate, graduate and professional degrees to students. Approximately 49,650 degrees were awarded in the 2002-03 school year. About 197,450 full-time students were enrolled at the nine UC campuses and the Hastings College of Law in the 2002-03 school year. The California State University System, provides undergraduate and graduate degrees to students. Approximately 76,755 degrees were awarded in the 2002-03 school year. About 331,400 full-time students were enrolled at the 23 campuses in the 2002-03 school year. The third sector consists of 108 campuses operated by 72 community college districts which provide associate degrees and certificates to students. Additionally students may attend community colleges to meet basic skills and other general education requirements prior to transferring to a four-year undergraduate institution. Approximately 118,000 associate degrees and certificates were awarded in the 2002-03 school year. About 1.7 million students were enrolled in California's community colleges in the spring of 2003.

Employee Relations

In 2003-04, the State work force is comprised of approximately 318,000 personnel years, of which approximately 116,000 personnel years represent employees of institutions of higher education. Of the remaining 202,000 personnel years, approximately 166,000 are subject to collective bargaining and approximately 36,000 are excluded from collective bargaining. State law provides that State employees, defined as any civil service employee of the State and teachers under the jurisdiction of the Department of Education or the Superintendent of Public Instruction, and excluding certain other categories, have a right to form, join, and participate in the activities of employee organizations for the purpose of representation on all matters of employer-employee relations. The chosen employee organization has the right to represent its members, except that once an employee organization is recognized as the exclusive representative of a bargaining unit, only that organization may represent employees in that unit.

The scope of representation is limited to wages, hours, and other terms and conditions of employment. Representatives of the Governor are required to meet and confer in good faith and endeavor to reach agreement with the employee organization, and, if agreement is reached, to prepare a memorandum of understanding and present it to the Legislature for ratification. The Governor and the recognized employee organization are authorized to agree mutually on the appointment of a mediator for the purpose of settling any disputes between the parties, or either party could request the Public Employment Relations Board to appoint a mediator.

State employees are represented by 21 collective bargaining units. The State recently signed Memoranda of Understanding with 17 of these collective bargaining units to achieve current year savings in State personnel costs, a way of mitigating the State's difficult fiscal condition. Two of these contracts expire in June 2004, seven expire in June 2005, five expire in June 2006, and two expire in June 2008. Another collective bargaining unit is under contract until July 2006. The remaining four collective bargaining units, comprising less than 5 percent of the State workforce, do not have a signed contract; the terms of the prior agreements remain in effect. The Department of Personnel Administration (DPA) is continuing to negotiate with these units. The State has not experienced a major work stoppage since 1972. The California State Employees' Association (CSEA) is the exclusive representative for nine of the 21 collective bargaining units, or approximately 50 percent of those employees subject to collective bargaining. Each of the remaining exclusive representatives represents only one bargaining unit.

ECONOMY AND POPULATION

Introduction

California's economy, the largest among the 50 states and one of the largest in the world, has major components in high technology, trade, entertainment, agriculture, manufacturing, tourism, construction and services. In early 2001, California's economy slipped into a recession, which was concentrated in the State's high-tech sector and, geographically, in the San Francisco Bay Area. The economy has since stabilized with only 2,400 lost jobs between January 2002 and December 2003 compared with 290,000 lost jobs between March 2001 and January 2002. See "CURRENT STATE BUDGET—Economic Assumptions."

Population and Labor Force

The State's July 1, 2003 population of over 35 million represented over 12 percent of the total United States population.

California's population is concentrated in metropolitan areas. As of the April 1, 2000 census, 97 percent resided in the 25 Metropolitan Statistical Areas in the State. As of July 1, 2002, the 5-county Los Angeles area accounted for 49 percent of the State's population, with over 17.0 million residents, and the 10-county San Francisco Bay Area represented 20 percent, with a population of over 7.0 million.

The following table shows California's population data for 1994 through 2003.

TABLE 14
Population 1994-2003[(a)]

Year	California Population	% Increase Over Preceding Year	United States Population	% Increase Over Preceding Year	California as % of United States
1994	31,523,080	0.7%	263,125,821	1.2%	12.0%
1995	31,711,094	0.6	266,278,393	1.2	11.9
1996	31,962,050	0.8	269,394,284	1.2	11.9
1997	32,451,746	1.5	272,646,925	1.2	11.9
1998	32,861,779	1.3	275,854,104	1.2	11.9
1999	33,417,247	1.7	279,040,168	1.2	12.0
2000	34,040,489	1.9	282,177,754	1.1	12.1
2001	34,726,513	2.0	285,093,813	1.0	12.2
2002	35,336,138	1.8	287,973,924	1.0	12.3
2003	35,933,943	1.7	290,809,777	1.0	12.4

(a) Population as of July 1.

Source: U. S. figures from U.S. Department of Commerce, Bureau of the Census; California figures from State of California, Department of Finance.

The following table presents civilian labor force data for the resident population, age 16 and over, for the years 1994 to 2003.

TABLE 15
Labor Force 1994-2003
(Thousands)

Year	Labor Force	Employment	Unemployment Rate (%) California	Unemployment Rate (%) United States
1994	15,294	13,979	8.6%	6.1%
1995	15,236	14,040	7.8	5.6
1996	15,371	14,261	7.2	5.4
1997	15,786	14,792	6.3	4.9
1998	16,138	15,181	5.9	4.5
1999	16,376	15,522	5.2	4.2
2000	16,892	16,057	4.9	4.0
2001	17,172	16,249	5.4	4.7
2002	17,376	16,215	6.7	5.8
2003[a]	17,460	16,283	6.7	6.0

(a) Preliminary.

Source: State of California, Employment Development Department.

Employment, Income, Construction and Export Growth

The following table shows California's non-agricultural employment distribution and growth for 1993 and 2003.

TABLE 16
Payroll Employment By Major Sector
1993 and 2003

Industry Sector	Employment (Thousands) 1993	Employment (Thousands) 2003	% Distribution of Employment 1993	% Distribution of Employment 2003
Trade, Transportation and Utilities	2,337.6	2,722.0	19.4%	18.9%
Government				
Federal Government	336.2	258.7	2.8	1.8
State and Local Government	1,744.4	2,167.7	14.5	15.0
Professional and Business Services	1,541.6	2,108.1	12.8	14.6
Manufacturing				
Nondurable goods	613.4	563.1	5.1	3.9
High Technology	523.2	399.5	4.4	2.8
Other Durable Goods	558.6	582.3	4.6	4.0
Educational and Health Services	1,195.8	1,536.3	9.9	10.7
Leisure and Hospitality	1,124.5	1,397.6	9.3	9.7
Financial Activities	787.0	886.8	6.5	6.2
Construction	458.9	788.8	3.8	5.5
Other Services	408.2	505.8	3.4	3.5
Information	386.2	471.4	3.2	3.3
Natural Resources and Mining	29.8	22.1	0.3	0.1
TOTAL NON-AGRICULTURAL	12,045.4	14,410.2	100%	100%

Source: State of California, Employment Development Department.

The following tables show California's total and per capita income patterns for selected years.

TABLE 17
Total Personal Income in California 1994-2003[(a)]

Year	Millions	% Change[(b)]	California % of U.S.
1994[(c)]...........	$ 735,104	2.9%	12.5%
1995..............	771,470	4.9	12.5
1996..............	812,404	5.3	12.4
1997..............	861,557	6.1	12.4
1998..............	931,564	8.1	12.6
1999..............	995,326	6.8	12.8
2000..............	1,100,679	10.6	13.1
2001..............	1,129,868	2.7	13.0
2002..............	1,155,247	2.2	13.0
2003[(d)]...........	1,199,000	3.8	13.1

(a) Bureau of Economic Analysis (BEA) estimates as of April 2003.
(b) Change from prior year.
(c) Reflects Northridge earthquake, which caused an estimated $15 billion drop in personal income.
(d) Estimated by California Department of Finance.

Note: Omits income for government employees overseas.

Source: U.S. Department of Commerce, BEA, State of California, Department of Finance.

TABLE 18
Per Capita Personal Income 1994-2003[(a)]

Year	California	% Change[(b)]	United States	% Change[(b)]	California % of U.S.
1994[(c)]	$23,348	2.3%	$22,340	3.7%	104.5%
1995	24,339	4.2	23,255	4.1	104.7
1996	25,373	4.2	24,270	4.4	104.5
1997	26,521	4.5	25,412	4.7	104.4
1998	28,240	6.5	26,893	5.8	105.0
1999	29,712	5.2	27,880	3.7	106.6
2000	32,363	8.9	29,760	6.7	108.7
2001	32,655	0.9	30,413	2.2	107.4
2002	32,898	0.7	30,832	1.4	106.7
2003[(d)]	33,367	1.4	31,552	2.3	105.8

(a) BEA's estimates as of April 2003.
(b) Change from prior year.
(c) Reflects Northridge earthquake, which caused an estimated $15 billion drop in personal income.
(d) Estimated by California Department of Finance.

Note: Omits income for government employees overseas.

Source: U.S. Department of Commerce, BEA, State of California, Department of Finance.

The following tables show California's residential and non-residential construction.

TABLE 19
Residential Construction Authorized by Permits

Year	Units			Valuation[a]
	Total	Single	Multiple	(millions)
1995	85,293	68,689	16,604	$13,879
1996	94,283	74,923	19,360	15,289
1997	111,716	84,780	26,936	18,752
1998	125,707	94,298	31,409	21,976
1999	140,137	101,711	38,426	25,783
2000	148,540	105,595	42,945	28,142
2001	148,757	106,902	41,855	28,804
2002	167,761	123,865	43,896	33,305
2003[b]	195,448	138,861	56,587	38,923

(a) Valuation includes additions and alterations.
(b) Preliminary.

Source: Construction Industry Research Board

TABLE 20
Nonresidential Construction
(Thousands of dollars)

Year	Commercial	Industrial	Other	Additions and Alterations	Total
1995	$2,308,911	$ 732,874	$1,050,693	$4,062,273	$ 8,154,751
1996	2,751,925	1,140,574	1,152,443	4,539,219	9,584,161
1997	4,271,378	1,598,428	1,378,220	5,021,792	12,269,818
1998	5,419,251	2,466,530	1,782,337	5,307,901	14,976,019
1999	5,706,719	2,256,166	2,350,213	6,269,194	16,582,292
2000	6,962,031	2,206,169	2,204,754	7,252,004	18,624,958
2001	6,195,368	1,552,047	2,584,321	6,421,551	16,753,287
2002	5,195,348	1,227,754	2,712,681	5,393,329	14,529,112
2003[a]	4,039,229	1,320,222	2,946,004	5,603,087	13,908,542

(a) Preliminary.

Source: Construction Industry Research Board

The following table shows California's export growth for the period from 1996 through 2003.

TABLE 21
Exports Through California Ports
(In millions)

Year	Exports[(a)]	% Change
1996	$124,120.0	6.2%
1997	131,142.7	5.7
1998	116,282.4	-11.3
1999	122,092.8	5.0
2000	148,554.6	21.7
2001	127,255.3	-14.3
2002	111,340.1	-12.5
2003	113,550.7	2.0

(a) "Free along ship" Value Basis

Source: U.S. Department of Commerce, Bureau of the Census

LITIGATION

The State is a party to numerous legal proceedings. The following are the most significant pending proceedings, as reported by the Office of the Attorney General. See "LITIGATION" in the main body of the Official Statement.

Challenges Related to the Vehicle License Fee Offset and Related Payments to Local Governments

State law establishes an excise tax on motor vehicles and manufactured homes in the amount of two percent (2%) of the vehicle's or home's fair market value. In 1999, pursuant to Revenue and Taxation Code section 10754, the Legislature adopted successive offsets to the vehicle license fee paid by vehicle owners and mobile home owners. As a result of these offsets, the State transferred money each month from the General Fund to local governments in the amount of the cumulative offsets.

In June 2003, the Davis Administration determined that there were insufficient moneys available to be transferred from the General Fund to fund vehicle license fee offset payments the State was making to local governments. See "STATE FINANCES – Local Governments – Vehicle License Fee." This caused the State Department of Motor Vehicles and the State Department of Housing and Community Development to discontinue the offsets and, correspondingly, the amount of vehicle license fees paid by vehicle owners and mobile home owners increased.

Shortly after taking office on November 17, 2003, the Governor issued Executive Order S-1-03, rescinding the Davis Administration's action and directing the Department of Motor Vehicles to reinstate the General Fund offset to the vehicle license fee provided in Revenue and Taxation Code Section 10754 "as soon as administratively feasible." By subsequent administrative action, the Administration adjusted current year expenditures in order to commence transfers from the General Fund to local governments in the amount of the offsets.

These various actions have given rise to the following litigation:

On July 1, 2003, several plaintiffs, including several Republican legislators and a non-profit public interest group, filed *Howard Jarvis Taxpayers Association, et al. v. California Department of Motor Vehicles* (Sacramento County Superior Court, Case No. 03AS03665), in which plaintiffs seek declaratory relief based on several theories, each of which would find the Davis Administration's discontinuation of the offset invalid. The State demurred to plaintiffs' second amended complaint, stating that it fails to state a cause of action. The court sustained the demurrer without leave to amend and, on February 16, 2004, entered a judgment dismissing this action. It is not yet known whether the plaintiffs intend to appeal.

On January 21, 2004, an original proceeding, *University of California Students Association, et al., v. Governor Arnold Schwarzenegger, et al.* (Case No. S122032), was instituted in the California Supreme Court. The petition for writ of mandate claims there were insufficient moneys in the General Fund available to reinstate the vehicle license fee offsets, and that the State cannot reduce appropriations to various programs in order to make offset-related transfers to local governments. Petitioners ask the Supreme Court to issue a writ commanding various State officers that they may not enforce Executive Order S-1-03, and ordering them to refrain from implementing any appropriation reductions made for the purpose of funding offset-related transfers to local governments. On February 18, 2004, the Supreme Court denied the petition without prejudice to the commencement of any appropriate proceeding in the superior court. The petitioners have not filed any subsequent action.

On January 30, 2004, *Robert Brooks and David Gautreaux v. Governor Arnold Schwarzenegger* (Case No. BC309929) was filed in the Los Angeles County Superior Court. In this case, plaintiffs allege that the adjustments of current year expenditures made by the Administration in order to provide for the transfers to local governments violates the California Constitution, and ask the Court to enjoin the Director of Finance and the Controller from making offset-related payments to local governments until an appropriation for that purpose is made by the Legislature.

Bond-Related Matters

The Legislature established the Pension Obligation Bond Committee for the purpose, among others, of issuing bonds to fund all or a portion of the State's fiscal year 2003-04 employer obligation to the Public Employee's Retirement System. The Committee sought validation of the bonds and certain contracts pursuant to a validation process established by Code of Civil Procedure sections 860 et seq. in *Pension Obligation Bond Committee v. All Persons Interested in the Matter of the Validity of the State of California's Pension Obligation, etc.,* filed in the Sacramento County Superior Court. The trial court issued a judgment denying the Committee's request for validation of the bonds, and the case is currently on appeal before the Court of Appeal (Third District, Case No. CO45240). Briefing is underway, and no date for oral argument has been set.

The Legislature has adopted a statute (Stats. 2003, 1st Ex. Sess. 2003, ch.13) authorizing the establishment of the Fiscal Recovery Finance Authority for the purpose, among others, of issuing bonds to fund the State's accumulated budget deficit as of June 30, 2003. The amount of this accumulated budget deficit is identified by the Department of Finance to be approximately \$8.6 billion. On September 24, 2003, a complaint was filed in the Sacramento County Superior Court (*Fullerton Association of Concerned Taxpayers v. California Fiscal Recovery Financing Authority, et al.*, Case No. 93AS05319), seeking a declaration that any bonds issued pursuant to the statute without prior voter approval would violate the State constitutional debt limit and a determination that such bonds are invalid, and seeking an injunction against issuing bonds pursuant to the statute. This matter has not been served on any State officers. As a result of this action, the Fiscal Recovery Finance Authority filed a validation action pursuant to Code of Civil Procedure sections 860 et seq. in the same court (*California Fiscal Recovery Financing Authority v. All Persons Interested, etc.*; Case No. 03AS06875). Fullerton Association of Concerned Taxpayers, the plaintiff in the case filed in September, was the only party to answer the Fiscal Recovery Finance Authority's complaint. The Fullerton Association of Concerned Taxpayers has dismissed its action. The Fiscal Recovery Financing Authority's case has been set for trial on June 7, 2004.

Challenge Seeking Payment to Teacher's Retirement Board

In May 2003, the Legislature enacted legislation which reduces a continuing appropriation to the State Teacher's Retirement System's ("CalSTRS") Supplemental Benefit Maintenance Account ("SBMA") for fiscal year 2003-04 by $500 million. The legislative changes also provide that in future fiscal years, the $500 million may be returned if necessary to make the SBMA actuarially sound. On October 14, 2003, the CalSTRS board and certain CalSTRS members filed *Teacher's Retirement Board, as Manager of the California State Teachers, Retirement System, et al. v. Steve Peace, Director of California Department of Finance, and Steve Westly, California State Controller,* in the Sacramento County Superior Court (Case No. 03CS01503). This lawsuit seeks, primarily, a writ of mandate compelling the State Controller to transfer funds from the State's General Fund to the SBMA in an amount equal to the continuing appropriation as it existed prior to the enactment of the May legislation. It also seeks injunctive and declaratory relief to the same effect. Trial is currently scheduled to begin on May 21, 2004

Actions Seeking Flood-Related Damages

In January of 1997, California experienced major flooding with preliminary estimates of property damage of approximately $1.6 to $2.0 billion. In *McMahan v. State*, (Sacramento County Superior Court, Case No. 02-AS-06058), a substantial number of plaintiffs have joined suit against the State, local agencies, and private companies and contractors seeking compensation for the damages they suffered as a result of the flooding. A trial date has been scheduled for October 24, 2004. The State is vigorously defending the action.

Paterno v. State of California (Yuba County Superior Court, Judicial Counsel Coordination Proceeding 2104) is a coordinated action involving 3,000 plaintiffs seeking recovery for damages caused by the Yuba River flood of February 1986. The trial court found liability in inverse condemnation and awarded damages of $500,000 to a sample of plaintiffs. The State's potential liability to the remaining plaintiffs ranges from $800 million to $1.5 billion. In 1992, the State and plaintiffs filed appeals of the decision in the sample plaintiffs' action, and upon remand, plaintiffs' inverse condemnation cause of action was re-tried. The trial court ruled in favor of the State as to all plaintiffs. The appellate court reversed the trial court judgment and remanded the case to the trial court with directions to enter judgment in favor of plaintiffs and ordered the State to pay costs on appeal and costs of suit, including reasonable attorney, appraisal and engineering fees actually incurred. On March 17, 2003, the Supreme Court denied the State's petition for review (California Supreme Court, Case No. S121713) of the appellate court's decision. That denial brought the liability phase of this litigation to a close. The issues of damages, interest, fees, costs and expenses are being litigated in the Yuba County Superior Court.

Tax Refund Cases

In *Farmer Brothers Company v. Franchise Tax Board*, the trial court determined that Revenue and Taxation Code section 24402 ("Section 24402"), which establishes a corporate tax deduction for received dividends, to the extent such dividends are based on the dividend-paying corporation's income subject to California franchise taxes, violates the commerce clause of the United States Constitution. That decision was affirmed on appeal (Second Appellate District, Case No. B160061), and the California Supreme Court denied the Franchise Tax Board's petition for review. The United States Supreme Court denied the Franchise Tax Board's petition for certiorari on February 23, 2004, bringing the case to a close.

Three pending cases also allege that Section 24402 violates the commerce clause. *Montgomery Ward LLC v. Franchise Tax Board* is pending in the San Diego Superior Court (Case No. 802767). In *General Motors Corp. v. Franchise Tax Board* (Court of Appeal, Second Appellate District, Case No. B165665) and in *Microsoft Corporation v. Franchise Tax Board* (Court of Appeal, First Appellate District, Case No. A105312), the Franchise Tax Board is appealing adverse trial court judgments. In *General Motors,* the appellate court heard oral argument on March 25, 2004.

Six pending cases challenge the Franchise Tax Board's treatment of receipts from investment of cash in short-term financial instruments, and the resulting impact on the apportionment of corporate income allegedly earned outside of California to the corporation's California tax obligation. Three of these cases (*Montgomery Ward, General Motors, and Microsoft*) are also cases in which Revenue and Tax Code section 24402 has been challenged, as discussed in the previous paragraph. *Montgomery Ward LLC v. Franchise Tax Board* is pending in the San Diego Superior Court (Case No. 802767), and *Colgate-Palmolive v. Franchise Tax Board* is pending in the Sacramento County Superior Court (Case No. 03AS00707). *The Limited Stores, Inc. and Affiliates v. Franchise Tax Board* is pending in the Court of Appeal, First Appellate District (Case No. A102915); *General Motors Corp. v. Franchise Tax Board* is pending in the Court of Appeal, Second Appellate District (Case No. B165665) and oral argument was heard in that case on March 25, 2004; *Toys "R" Us, Inc. v. Franchise Tax Board* is pending in the Court of Appeal, Third Appellate District (Case No. C045386); and *Microsoft Corporation v. Franchise Tax Board* is pending in the Court of Appeal, First Appellate District (Case No. A105312). The trial courts in *The Limited Stores, General Motors* and *Toys "R" Us* ruled in favor of the Franchise Tax Board on this issue; and in *Microsoft Corporation*, the trial court ruled against the Franchise Tax Board. Other taxpayers have raised this same issue in administrative actions. A final decision in favor of any of these plaintiffs could result in tax refunds to similarly situated taxpayers in an amount exceeding $500 million, with a potential future annual revenue loss of $50 million. The State is vigorously litigating this issue.

In *Eisenhower Medical Center, et al. v. State Board of Equalization* (San Francisco Superior Court, Case No. 994985), 117 hospitals claim that certain intravenous sets and diagnostic substances are "medicines" within the meaning of the Revenue and Tax Code, and thus are exempt from sales and use taxes. The State Board of Equalization ("SBE") does not consider intravenous sets (other than those used primarily for enteral feeding) and diagnostic substances to be medicines and, therefore, those items are subject to sales and use taxes. The trial court ruled in favor of the SBE, and an appeal is expected. Due to a retroactive regulatory change that the SBE adopted during the pendency of this case, specified types of enteral feeding supplies are now exempt from sales and use taxes. Therefore, even if the State prevails on appeal, refunds will be required in the amount of up to $5 million. Should the plaintiffs ultimately prevail on all contested issues, estimated refunds to plaintiffs and others similarly situated hospitals would total approximately $400 million and estimated future revenue loss would be $70 million per year.

In *County of Orange v. Orange County Assessment Appeals Board #3; Bezaire, et al., Real Parties in Interest*, (Court of Appeal, Fourth Appellate District, Division 3, Case No. G032412), the trial court determined that the Orange County assessor's office received property taxes from two taxpayers in excess of the amounts collectable under Article XIII A of the California Constitution (implemented in 1978 by Proposition 13). The plaintiffs' legal claim focuses on the constitutionality of the practice of the Orange County assessor's office to increase or "recapture" the assessed values of real properties that temporarily decline and then increase in value. On March 26, 204, in a unanimous decision certified for publication, the Court of Appeal reversed the ruling of the trial court and directed that judgment be entered in favor of the County of Orange. It is not yet known whether the plaintiffs will seek review of this decision. The effects of a final determination by an appellate court that the Orange County assessor's office's contested assessment practices are contrary to Proposition 13 could result in an increase in the State general fund component of the financing guarantee to public schools established by Proposition 98 (see "STATE FINANCES—Proposition 98") in an amount in excess of several billion dollars.

Environmental Cleanup Matter

In a federal Environmental Protection Agency ("U.S. EPA") administrative abatement action entitled *In the Matter of: Leviathan Mine, Alpine County, California, Regional Water Quality Control Board, Lahontan Region, State of California* (U.S. EPA Region IX CERCLA Docket No. 00-16(a)), the State, as owner of the Leviathan Mine, is a party through the Lahontan Regional Water Quality Control Board ("Board"), which is the State entity potentially responsible for performing certain environmental remediation at the Leviathan Mine site. Also a party is ARCO, the successor in interest to the mining company that caused certain pollution of the mine site. The Leviathan Mine site is listed on the U.S. EPA "Superfund" List, and both remediation costs and costs for Natural Resource Damages may be imposed on the State. The Board has undertaken certain remedial action at the mine site, but the U.S. EPA's decision on the interim and final remedies are pending. ARCO has filed several state law claims against the State with the California Victim Compensation and Government Claims Board (an administrative agency with which certain claims must be filed as a prerequisite to litigation seeking damages against the State which was formerly named the Board of Control, the "Government Claims Board"), but litigation on these claims have been tolled by agreement of the parties until at least October, 2004. It is possible these matters could result in a potential loss to the State in excess of $400 million.

Energy-Related Matters

In *People v. ACN Energy, Inc., et al.* (Sacramento County Superior Court, Case No. 01AS05497), the court is considering whether and to what extent compensation is due to market participants which have claimed compensation as a result of the Governor's issuance of executive orders, under the California Emergency Service Act, "commandeering" power purchase arrangements held by Pacific Gas & Electric Company ("PG&E") and Southern California Edison ("SCE"), referred to as "block forward contracts." In this action the State seeks a declaration that the State is not liable for damages as a result of these orders, nor for compensation for inverse condemnation, and that any damages suffered by any of the defendants is offset by payments made by the Department of Water Resources for electricity received under the "commandeered" "block forward contracts." Complaints and cross-complaints for inverse condemnation, recovery under the Emergency Services Act and other causes of action brought by PG&E, Reliant Energy Services, Dynegy Power Marketing, Williams Energy Services, Sempra Energy Trading, the California Power Exchange, Mirant Americas Energy, Duke Energy Trading and Marketing, and numerous other market participants have been joined with the declaratory relief action in Judicial Council Coordination Proceeding No. 4203, in Sacramento County Superior Court. In an administrative proceeding action before the Government Claims Board (which was dismissed on procedural grounds), the California Power Exchange stated claims for "commandeering" the "block forward contracts" in the amount of approximately $1 billion.

Pacific Gas and Electric Company v. The State of California is now pending in the Court of Appeal, Third Appellate District (Case No. C043507). In the trial court, PG&E filed a complaint for breach of contract alleging that statutes enacted in 1996 as part of the restructuring of the electric power industry in California ("AB 1890") established a "regulatory contract" between the State and PG&E that authorized PG&E to sell the output of its retained generation facilities in interstate power markets at prices regulated by FERC and to sell the facilities themselves, and that by amending AB 1890 in 2001, the State deprived PG&E of the right to such sales and thereby breached that "regulatory contract." PG&E's complaint sought damages in an amount to be proven, but in an administrative proceeding before the Government Claims Board, in which PG&E's claims were denied, PG&E sought damages of at least $4.3 billion to compensate for the losses alleged in this action. The trial court sustained the demurrer of the State without leave to amend, dismissing the lawsuit. The pending action is PG&E's appeal of that dismissal.

Escheated Property Claims

In five pending cases, plaintiffs claim that the State Controller has a constitutional and statutory duty to give notice prior to the time the Controller sells property that has escheated to the State (in these cases, shares of stock): *Fong v. Westly* (Court of Appeal, Third District, Case No. C042007); *Harris v. Connell* (Court of Appeal, Second District, Case No. B160741); *Lusby-Taylor v. Connell* (U.S. Court of Appeals for the Ninth Circuit, Case No. 02-16511); *Orfield v. Connell* (Los Angeles County Superior Court, Case No. BC288429); and *Suever v. Connell* (U.S. Court of Appeals for the Ninth Circuit, Case No. 04-15555). The plaintiffs also claim that the Controller failed to comply with statutory notice requirements when it first received property that had escheated to the State. The plaintiffs seek damages, which the *Fong* plaintiffs have articulated as being in the amount of the difference between the amount they were paid for the stock upon its sale, and either the current value of the stock or the highest market value of the stock between the date the Controller sold the stock and the present. All of these cases, except *Fong,* are styled as class actions, though in *Lusby-Taylor* and *Harris*, that issue was not determined prior to the trial court decisions that are being appealed. If one or more of these cases are successful as a class action and the class ultimately prevails on the merits, damages for the class could be in excess of $500 million. The State has prevailed at the trial court in *Suever* and *Lusby-Taylor,* and at both the trial court and appellate court in *Fong* and *Harris*. It is not yet known whether the plaintiffs in *Fong* or *Harris* will seek review of the appellate court decision. *Orfield* is being litigated in the trial court. The State is vigorously defending all of these actions.

Action Seeking Damages for Alleged Violations of Privacy Rights

In *Gail Marie Harrington-Wisely, et al. v. State of California, et al.*, (Los Angeles County Superior Court, Case No. BC 227373), a proposed class action, plaintiffs seek damages for alleged violations of prison visitors' rights resulting from the Department of Corrections' use of a body imaging machine to search visitors entering state prisons for contraband. If this action is certified as a class action, and a court were to award damages pursuant to the California Civil Code for every use of the body imaging machine, damages could be as high as $3 billion. The State is vigorously defending this action.

Actions Seeking Program Modifications

In the following cases, plaintiffs seek court orders or judgments that would require the State to modify existing programs and, except as specified, do not seek monetary damages. Nevertheless, a judgment against the State in any one of these cases could require changes in the challenged program that could result in increased programmatic costs to the State in a future fiscal year in excess of $400 million. Alternatively, in some circumstances, it may be possible that a judgment against the State could be addressed by legislative changes to the program that would cost less.

In *Williams, et al., v. State of California, et al.*, (San Francisco County Superior Court, Case No. 312236), a class action for declaratory relief and injunction brought by public school students against the State, the Board of Education, and Department of Education and the Superintendent of Public Instruction, the class alleges inadequacies in the public education system and seeks a variety of programmatic changes to the system including elimination of some types of multi-track, year-round school schedules. The State is vigorously defending this action. Trial is expected to begin in January, 2005.

In *Natural Resources Defense Council et al., v. California Department of Transportation et al.*, (United States District Court, Central District, Case No. 93-6073-ER-(JRX)), plaintiffs obtained an injunction requiring the Department of Transportation (the "Department") to comply with National Pollution Discharge Elimination System ("NPDES") requirements under the federal Clean Water Act ("Act") in connection with storm water discharges from State highways and construction sites in an area that includes most of Los Angeles and Ventura Counties. There is an established dispute resolution procedure intended to resolve disputes without a return to federal court. Subsequent modifications of the injunction have provided for, among other things, studies of pilot projects to address control of the sources of storm water pollution and the performance of studies of pilot projects to retrofit highways with storm water pollution control facilities. There has been no agreement regarding what measures arising out of the pilot projects and studies will be implemented. Plaintiffs' position is that the Department should be required to retrofit its facilities to treat storm water, regardless of whether any construction is otherwise planned in any given area. For planning purposes, the Department is including an additional 3 percent in the cost of future statewide construction and maintenance projects to pay for compliance measures. This 3 percent increase amounts to $500 million through fiscal year 2006-07. While the impact of a judgment of the scope sought by plaintiffs is difficult to determine, it is possible that a judgment that would require the State to retrofit all its highway facilities throughout the State could cost billions of dollars.

The following cases seek reforms to State programs for the treatment of institutionalized disabled persons. Some rough estimates suggest the financial impact of a judgment against the State defendants in any of these cases could be as high as $1 billion per year in programmatic costs going forward. The State is vigorously defending these actions.

In *Stephen Sanchez, et al. v. Grantland Johnson, et al.*, (U.S. Court of Appeals for the Ninth Circuit, Case No 04-15228), the plaintiffs have appealed a decision by the U.S. District Court dismissing plaintiffs' class action seeking declaratory and injunctive relief. The plaintiffs sought relief, alleging, in part, that provider rates for community-based services for developmentally disabled individuals are discriminatory under the ADA, and violate the Social Security Act, Civil Rights Act and the Rehabilitation Act, because they result in unnecessary institutionalization of developmentally disabled persons.

In *Capitol People First v. Department of Developmental Services* (Alameda County Superior Court, Case No. 2002-038715) a consortium of state and national law firms and public-interest groups brought suit against the Departments of Finance, California Department of Developmental Services and California Department of Health Services, alleging violations of the Lanterman Act, the ADA, and section 504 of the Rehabilitation Act by defendants needlessly isolate thousands of people with developmental disabilities in large facilities. The case seeks sweeping reforms, including requiring the State to offer a full range of community-based services.

Local Government Mandate Claims and Actions

In a test claim filed by the County of San Bernardino, now pending before the Commission on State Mandates (the "Commission") (Medically Indigent Adults, 01-TC-26 County of San Bernardino, Claimant, Statutes 1982, Chapters 328 and 1594), the Commission is being asked to determine the costs incurred by the county to provide state-mandated care of medically indigent adults ("MIAs"). The amount demanded in the claim for unreimbursed costs for fiscal year 2000-2001 is just over $9.2 million.

The County of San Bernardino's test claim poses a potential for a negative impact on the General Fund in the amount of the unreimbursed costs for all similarly situated county claimants for a period of years, as determined by the Commission. Certain estimates of the annual cost of the services rendered by all counties to MIAs exceed $4 billion. How much of that will be determined to be "unreimbursed" to the counties by the State is unknown.

Currently the counties receive approximately $1.4 billion annually in vehicle license fee revenue and $2.3 billion annually in sales tax revenue to fund various social services, public health and mental health programs, which include the programs that provide services to MIAs. The State law that authorized the transfer of the vehicle license fee portion of this revenue to the counties and the authority to transfer the revenue to the counties were repealed as a result of a final appellate court decision (*County of San Diego v. Commission on State Mandates et al.* D039471; petition for review denied by the California Supreme Court) that awarded the County of San Diego $3.4 million for medical services rendered to MIAs during a two-year period. The finality of the *County of San Diego* decision caused the activation of automatic provisions of State law. In response to the automatic revenue reduction, the Department of Motor Vehicles promulgated emergency regulations that act to offset the reduction in revenues. Those regulations are scheduled to expire on July 1, 2004. The Department of Motor Vehicles is seeking to promulgate final regulations to address the effect of the reduction of revenues, and, as presently proposed, such regulations would act to retain the amount of vehicle license fees paid to counties. Legislation is currently pending to reinstate the authority to transfer the vehicle license fee revenues to the counties. See "STATE FINANCES -- Local Governments -- Vehicle License Fee." The sales tax revenue made available to the counties may be reduced as a result of existing statutory provisions that would redirect those funds upon a finding by the Commission that these mandates are unfunded in an annual amount of $1 million or more.

Six matters are pending that challenge the State's practice of deferring payments to local governments for certain state-mandated services and programs by making a budgetary appropriation of $1,000 for each program, statewide. Two matters, pending in the San Diego County Superior Court (*County of San Diego v. State of California, et al.,* Case No. GIC 825109; and *County of Orange v. State of California, et al.* Case No. GIC 827845), allege that the State's practice of deferring payments to local governments is unconstitutional. These actions seek a declaration that the State is constitutionally and statutorily obligated to promptly and fully reimburse the counties, and seek reimbursement for mandated costs. The *County of San Diego* matter seeks reimbursement in an amount in excess of $40 million. Four matters are pending in the Sacramento County Superior Court (*County of San Diego v. State of California, et al.,* Case No. 04AS00371; *County of Orange v. Stae of California, et al.,* Case No. 04AS01341; *Sacramento County v. State of California, et al.,* Case No. 04AS01355; and *County of Contra Costa v. State of California, et al.,* Case No. 04AS01039), which make similar allegations as to the State's statewide appropriation for a program to provide services to handicapped and seriously emotionally disturbed students. The counties seek reimbursement for program costs, and declarations that until such time as reimbursement is received, they are excused from providing services or incurring costs in relation to the program. The *County of San Diego* matter seeks reimbursement in the amount of approximately $9 million for this program. The effects of a final determination by an appellate court that the contested appropriation practices are unconstitutional or that the State is required to appropriate an amount equal to the amount of the mandated costs, if applied to each of California's 58 counties, could result in costs in excess of $1.5 billion.

Reparations Claim

On July 15, 2003, the matter of *Emilia Castaneda v. State of California, et al.* was filed in the Los Angeles County Superior Court (Case No. BC299062). The class action complaint alleges illegalities associated with the repatriation of Mexican Americans during the 1930's and 1940's, and names the State of California, County of Los Angeles, City of Los Angeles and Los Angeles Chamber of Commerce as defendants. Plaintiff claims the class consists of "approximately 400,000 American citizens and resident aliens who were wrongfully expelled from California because of their Mexican ancestry." The complaint alleges causes of action for unlawful race discrimination, conspiracy to deprive plaintiffs of their civil rights, violations of due process, denial of equal protection, unjust taking of property, violation of freedom of association, and violation of the right to travel. The State is vigorously defending this case. The amount of any potential impact this case may have on the General Fund is unclear because it is unclear whether any claims can be brought within the applicable statute of limitations.

On October 12, 2003, Governor Gray Davis vetoed Senate Bill 933, which would have provided that United States citizens or legal residents of Mexican descent who were coerced, forced, or falsely induced to emigrate from California during the period from 1929 to 1944, could seek recovery of damages, and that any such action brought on or before December 31, 2006, would not have been dismissed for failure to comply with the applicable statute of limitations.

Action for Damages for Alleged Destruction at Indian Burial Sites

On January 16, 2004, *John Tommy Rosas v. United States of America, et al.* was filed in the United States District Court, Central District of California (Case No. CV04-312 WMB (SSx)). Plaintiff, in his individual capacity and as vice-chairman of the Tribal Counsel, Gabrielino/Tongva Indians of California, alleges violation of various federal statutes by a variety of federal agencies, corporations, individuals and four State entities (the California Coastal Commission, the Regional Water Quality Control Board, the State Historic Preservation Officer and the California Native American Heritage Commission). Plaintiff alleges that in allowing the development of certain property, defendants violated federal laws protecting sacred Indian burial sites. Plaintiff seeks damages in the amount of $525 million. The State is in the process of assessing these allegations.

STATE DEBT TABLES

The tables which follow provide information on outstanding State debt, authorized but unissued general obligation bonds and commercial paper notes, debt service requirements for State general obligation and lease-purchase bonds, and authorized and outstanding State revenue bonds. For purposes of these tables, "General Fund bonds," also known as "non-self liquidating bonds," are general obligation bonds expected to be paid from the General Fund without reimbursement from any other fund. Although the principal of general obligation commercial paper notes in the "non-self liquidating" category is legally payable from the General Fund, the State expects that principal of such commercial paper notes will be paid only from the issuance of new commercial paper notes or the issuance of long-term general obligation bonds to retire the commercial paper notes. Interest on "non-self liquidating" general obligation commercial paper notes is payable from the General Fund.

"Enterprise Fund bonds," also known as "self liquidating bonds," are general obligation bonds for which program revenues are expected to be sufficient to reimburse in full the General Fund for debt service payments, but any failure to make such a reimbursement does not affect the obligation of the State to pay principal and interest on the bonds from the General Fund.

On April 7, 2004, the State Public Works Board issued $280,085,000 of lease revenue bonds. The State Public Works Board expects to issue approximately $492,240,000 of additional lease revenue bonds in April 2004.

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AUTHORIZED AND OUTSTANDING GENERAL OBLIGATION BONDS

As of March 1, 2004
(Thousands)

	Voter Authorization Date	Voter Authorization Amount	Bonds Outstanding (a)	CP Program Authorized (b)	Unissued (c)
GENERAL FUND BONDS (Non-Self Liquidating)					
California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Act of 2002	3/5/2002	$ 2,600,000	$ 219,360	$ 1,350,510	$ 1,030,130
California Library Construction and Renovation Bond Act of 1988	11/8/1988	75,000	46,520	0	2,595
California Library Construction and Renovation Bond Act of 2000	3/7/2000	350,000	4,530	47,350	298,100
California Park and Recreational Facilities Act of 1984	6/5/1984	370,000	116,940	n.a.	1,100
California Parklands Act of 1980	11/4/1980	285,000	25,795	n.a.	0
California Safe Drinking Water Bond Law of 1976	6/8/1976	175,000	37,030	n.a.	2,500
California Safe Drinking Water Bond Law of 1984	11/6/1984	75,000	22,195	n.a.	0
California Safe Drinking Water Bond Law of 1986	11/4/1986	100,000	57,335	n.a.	0
California Safe Drinking Water Bond Law of 1988	11/8/1988	75,000	48,980	5,100	2,000
California Wildlife, Coastal, and Park Land Conservation Act of 1988	6/7/1988	776,000	392,465	n.a.	7,330
Class Size Reduction Public Education Facilities Bond Act of 1998 (Hi Ed)	11/3/1998	2,500,000	1,978,925	478,725	0
Class Size Reduction Public Education Facilities Bond Act of 1998 (K-12)	11/3/1998	6,700,000	6,218,750	207,560	0
Clean Air and Transportation Improvement Bond Act of 1990	6/5/1990	1,990,000	1,304,020	242,490	40,925
Clean Water and Water Conservation Bond Law of 1978	6/6/1978	375,000	29,770	n.a.	0
Clean Water and Water Reclamation Bond Law of 1988	11/8/1988	65,000	45,975	0	0
Clean Water Bond Law of 1970	11/3/1970	250,000	3,500	n.a.	0
Clean Water Bond Law of 1974	6/4/1974	250,000	7,665	n.a.	0
Clean Water Bond Law of 1984	11/6/1984	325,000	75,300	n.a.	0
Community Parklands Act of 1986	6/3/1986	100,000	37,695	n.a.	0
County Correctional Facility Capital Expenditure and Youth Facility Bond Act of 1988	11/8/1988	500,000	296,320	0	0
County Correctional Facility Capital Expenditure Bond Act of 1986	6/3/1986	495,000	196,955	n.a.	0
County Jail Capital Expenditure Bond Act of 1981	11/2/1982	280,000	49,375	n.a.	0
County Jail Capital Expenditure Bond Act of 1984	6/5/1984	250,000	46,400	n.a.	0
Earthquake Safety and Public Buildings Rehabilitation Bond Act of 1990	6/5/1990	300,000	204,750	59,450	0
Fish and Wildlife Habitat Enhancement Act of 1984	6/5/1984	85,000	22,135	n.a.	3,000
Hazardous Substance Cleanup Bond Act of 1984	11/6/1984	100,000	5,000	n.a.	0
Higher Education Facilities Bond Act of 1986	11/4/1986	400,000	115,850	n.a.	0
Higher Education Facilities Bond Act of 1988	11/8/1988	600,000	293,525	3,440	7,000
Higher Education Facilities Bond Act of June 1990	6/5/1990	450,000	250,830	2,130	0
Higher Education Facilities Bond Act of June 1992	6/2/1992	900,000	638,710	4,840	3,440
Housing and Emergency Shelter Trust Fund Act of 2002	11/5/2002	2,100,000	0	980,000	1,120,000
Housing and Homeless Bond Act of 1990	6/5/1990	150,000	6,400	n.a.	0
Kindergarten - University Public Education Facilities Bond Act of 2002 (K-12)	11/5/2002	11,400,000	6,408,745	4,991,255	0
Kindergarten - University Public Education Facilities Bond Act of 2002 (Hi-Ed)	11/5/2002	1,650,000	15,320	266,680	1,368,000
Lake Tahoe Acquisitions Bond Act	8/2/1982	85,000	25,240	n.a.	0

AUTHORIZED AND OUTSTANDING GENERAL OBLIGATION BONDS
(Continued)

	Voter Authorization		Bonds	CP Program	
	Date	Amount	Outstanding (a)	Authorized (b)	Unissued (c)
New Prison Construction Bond Act of 1981	6/8/1982	$ 495,000	$ 39,250	$ n.a.	$ 0
New Prison Construction Bond Act of 1984	6/5/1984	300,000	32,500	n.a.	0
New Prison Construction Bond Act of 1986	11/4/1986	500,000	155,595	n.a.	1,500
New Prison Construction Bond Act of 1988	11/8/1988	817,000	399,810	12,260	0
New Prison Construction Bond Act of 1990	6/5/1990	450,000	229,560	6,125	0
Passenger Rail and Clean Air Bond Act of 1990	6/5/1990	1,000,000	577,810	10,565	0
Public Education Facilities Bond Act of 1996 (K-12)	3/26/1996	2,025,000	1,703,545	46,790	0
Public Education Facilities Bond Act of 1996 (Hi-Ed)	3/26/1996	975,000	866,605	29,630	8,700
1988 School Facilities Bond Act	11/8/1988	800,000	417,480	2,665	0
1990 School Facilities Bond Act	6/5/1990	800,000	439,750	2,990	0
1992 School Facilities Bond Act	11/3/1992	900,000	569,982	6,614	0
Safe, Clean Reliable Water Supply Act of 1996	11/5/1996	995,000	564,510	402,765	0
Safe Drinking Water Bond Act of 2000	3/7/2000	1,970,000	382,705	702,002	873,800
Safe Neighborhood Parks Bond Act of 2000	3/7/2000	2,100,000	871,765	682,015	528,805
School Building and Earthquake Bond Act of 1974	11/5/1974	40,000	30,655	n.a.	0
School Facilities Bond Act of 1988	6/7/1988	800,000	370,480	n.a.	0
School Facilities Bond Act of 1990	11/6/1990	800,000	475,170	2,550	0
School Facilities Bond Act of 1992	6/2/1992	1,900,000	1,169,040	17,290	0
Seismic Retrofit Bond Act of 1996	3/26/1996	2,000,000	1,601,865	269,645	0
Senior Center Bond Act of 1984	11/6/1984	50,000	7,250	n.a.	0
State School Building Lease-Purchase Bond Law of 1982	11/2/1982	500,000	18,210	n.a.	0
State School Building Lease-Purchase Bond Law of 1984	11/6/1984	450,000	102,100	n.a.	0
State School Building Lease-Purchase Bond Law of 1986	11/4/1986	800,000	260,150	n.a.	0
State, Urban, and Coastal Park Bond Act of 1976	11/2/1976	280,000	12,845	n.a.	0
Veterans' Homes Bond Act of 2000	3/7/2000	50,000	0	45,000	5,000
Voting Modernization Bond Act of 2002	3/5/2002	200,000	0	155,000	45,000
Water Conservation and Water Quality Bond Law of 1986	6/3/1986	150,000	65,970	n.a.	27,600
Water Conservation Bond Law of 1988	11/8/1988	60,000	37,255	6,266	5,234
Water Security, Clean Drinking Water, Coastal and Beach Protection Act of 2002	11/5/2002	3,440,000	413,645	918,455	2,107,900
Total General Fund Bonds		$ 62,828,000	$ 31,063,807	$ 11,958,157	$ 7,489,659
ENTERPRISE FUND BONDS (Self Liquidating)					
California Water Resources Development Bond Act of 1959	11/8/1960	$ 1,750,000	$ 788,420	$ n.a.	$ 167,600
Veterans Bonds	(d)	4,510,000	1,446,190	0	605,585
Total Enterprise Fund Bonds		$ 6,260,000	$ 2,234,610	$ 0	$ 773,185
TOTAL GENERAL OBLIGATION BONDS		$ 69,088,000	$ 33,298,417	$ 11,958,157	$ 8,262,844

(a) Includes the initial value of capital appreciation bonds rather than the accreted value.
(b) Represents the total amount of commercial paper authorized by Finance Committees that could be issued for new money projects. Of this amount, no more than $1.5 billion of commercial paper principal and interest can be owing at any time. Currently, there is $0.00 of commercial paper issued and outstanding. The bond acts marked as "n.a." are not legally permitted to utilize commercial paper, or all bonds were issued before the commercial paper program began.
(c) Treats full commercial paper authorization as issued; see footnote (b).
(d) Various dates.

SOURCE: State of California, Office of the Treasurer.

OUTSTANDING STATE DEBT
FISCAL YEARS 1998-99 THROUGH 2002-03
(Dollars in Thousands Except for Per Capita Information)

	1998-99	1999-00	2000-01	2001-02	2002-03
Outstanding Debt (a)					
General Obligation Bonds					
General Fund (Non-Self Liquidating)	$ 16,202,211	$ 17,869,616	$ 20,472,893	$ 22,115,362	$ 26,758,626
Enterprise Fund (Self Liquidating)	3,674,020	3,474,900	3,396,215	3,211,310	2,801,775
Total	$ 19,876,231	$ 21,344,516	$ 23,869,108	$ 25,326,672	$ 29,560,401
Lease-Purchase Debt	6,671,534	6,627,944	6,413,260	6,341,935	6,704,599
Total Outstanding General Obligation Bonds and Lease-Purchase Debt	$ 26,547,765	$ 27,972,460	$ 30,282,368	$ 31,668,607	$ 36,265,000
Bond Sales During Fiscal Year					
Non-Self Liquidating General Obligation Bonds	$ 2,650,000	$ 2,750,000	$ 4,419,665	$ 3,905,025	$ 5,150,000
Self Liquidating General Obligation Bonds	$ 351,500	$ 126,500	$ 358,625	$ 111,325	$ 0
Lease-Purchase Debt	$ 456,410	$ 293,235	$ 214,585	$ 229,105	$ 673,975
Debt Service (b)					
Non-Self Liquidating General Obligation Bonds	$ 1,934,628	$ 2,045,566	$ 2,279,636	$ 2,367,570	$ 1,738,740
Lease-Purchase Debt	$ 652,131	$ 654,485	$ 670,228	$ 647,568	$ 664,846
General Fund Receipts (b)	$ 58,510,860	$ 72,226,473	$ 78,330,406	$ 66,604,508	$ 78,587,019
Non-Self Liquidating General Obligation Bonds Debt Service as a Percentage of General Fund Receipts	3.31%	2.83%	2.91%	3.55%	2.21%
Lease-Purchase Debt Service as a Percentage of General Fund Receipts	1.11%	0.91%	0.86%	0.97%	0.85%
Population (c)	32,861,779	33,417,247	34,036,376	34,698,173	35,301,480
Non-Self Liquidating General Obligation Bonds Outstanding Per Capita	$ 493.04	$ 534.74	$ 601.50	$ 637.36	$ 758.00
Lease-Purchase Debt Outstanding Per Capita	$ 203.02	$ 198.34	$ 188.42	$ 182.77	$ 189.92
Personal Income (d)	$ 931,564,000	$ 995,326,000	$1,100,679,000	$1,129,868,000	$1,155,247,000
Non-Self Liquidating General Obligation Bonds Outstanding as Percentage of Personal Income	1.74%	1.80%	1.86%	1.96%	2.32%
Lease-Purchase Debt Outstanding as Percentage of Personal Income	0.72%	0.67%	0.58%	0.56%	0.58%

(a) As of last day of fiscal year. Includes the initial value of capital appreciation bonds rather than the accreted value.
(b) Calculated on a cash basis; debt service costs of bonds issued in any fiscal year largely appear in subsequent fiscal year.
(c) As of July 1, the beginning of the fiscal year.
(d) Source: U.S. Department of Commerce, Bureau of Economic Analysis, http://www.bea.doc.gov/
Annual Totals: "Pre-benchmark" Revisions: Released April 2003. California Department of Finance.

SOURCES: Population: State of California, Department of Finance
Personal Income: State of California, Department of Finance; United States, Department of Commerce, Bureau of Economic Analysis (BEA)
Outstanding Debt, Bonds Sales During Fiscal Year and Debt Service: State of California, Office of the Treasurer.
General Fund Receipts: State of California, Office of the State Controller.

SCHEDULE OF DEBT SERVICE REQUIREMENTS FOR GENERAL FUND GENERAL OBLIGATION BONDS (a)
(Non-Self Liquidating)
As of March 1, 2004

Fiscal Year Ending June 30	Current Debt			
	Interest	Principal (b)	Total	
2004	$ 366,208,116.45	$ 164,345,509.42	$ 530,553,625.87	(c)
2005	1,543,819,592.59	1,319,232,629.25	2,863,052,221.84	
2006	1,469,036,195.00	1,251,846,249.96	2,720,882,444.96	
2007	1,399,444,060.93	1,283,931,249.96	2,683,375,310.89	
2008	1,332,830,387.93	1,442,213,587.73	2,775,043,975.66	
2009	1,256,377,988.75	1,487,953,240.54	2,744,331,229.29	
2010	1,177,869,051.30	1,543,906,249.96	2,721,775,301.26	
2011	1,098,939,584.84	1,511,335,295.12	2,610,274,879.96	
2012	1,016,009,461.19	1,198,625,509.42	2,214,634,970.61	
2013	957,826,111.25	987,973,240.54	1,945,799,351.79	
2014	912,060,680.89	869,436,249.96	1,781,496,930.85	
2015	871,792,107.19	865,721,249.96	1,737,513,357.15	
2016	877,299,716.46	788,037,138.21	1,665,336,854.67	
2017	839,426,159.60	821,205,125.65	1,660,631,285.25	
2018	801,234,417.23	846,033,014.68	1,647,267,431.91	
2019	761,327,843.50	908,529,956.72	1,669,857,800.22	
2020	718,678,204.75	968,931,411.03	1,687,609,615.78	
2021	673,899,581.00	922,150,722.61	1,596,050,303.61	
2022	630,675,242.25	1,062,779,797.05	1,693,455,039.30	
2023	579,260,631.45	1,077,911,262.12	1,657,171,893.57	
2024	529,657,874.36	954,133,692.69	1,483,791,567.05	
2025	483,665,138.80	1,104,158,006.65	1,587,823,145.45	
2026	433,053,327.59	1,016,255,625.23	1,449,308,952.82	
2027	385,686,702.59	1,022,888,931.76	1,408,575,634.35	
2028	337,500,769.09	1,067,838,427.91	1,405,339,197.00	
2029	317,700,285.00	985,438,601.24	1,303,138,886.24	
2030	271,063,459.50	1,117,038,356.07	1,388,101,815.57	
2031	222,302,387.00	736,263,866.54	958,566,253.54	
2032	191,847,727.50	665,375,473.43	857,223,200.93	
2033	163,927,120.00	526,321,716.03	690,248,836.03	
2034	9,214,295.00	227,290,000.00	236,504,295.00	
Total	$ 21,229,634,220.98	$ 29,663,806,512.18	$ 53,374,735,608.42	

(a) Variable Rate Bonds interest cost is estimated at 3.30%.
(b) Includes scheduled mandatory sinking fund payments.
(c) Total represents the remaining debt service requirements from April 1, 2004 through June 30, 2004.

SOURCE: State of California, Office of the Treasurer.

SCHEDULE OF DEBT SERVICE REQUIREMENTS
FOR ENTERPRISE FUND GENERAL OBLIGATION BONDS
(Self Liquidating)
As of March 1, 2004

Fiscal Year Ending June 30	Current Debt Interest	Current Debt Principal (a)	Current Debt Total
2004	$ 52,093,157.12	$ 23,810,000.00	$ 75,903,157.12 (b)
2005	125,529,089.75	122,930,000.00	248,459,089.75
2006	116,735,431.00	124,500,000.00	241,235,431.00
2007	107,712,864.76	129,705,000.00	237,417,864.76
2008	97,875,136.04	136,770,000.00	234,645,136.04
2009	87,974,336.25	139,695,000.00	227,669,336.25
2010	78,587,639.05	118,565,000.00	197,152,639.05
2011	71,193,275.77	88,750,000.00	159,943,275.77
2012	65,825,233.50	124,660,000.00	190,485,233.50
2013	60,033,305.62	119,420,000.00	179,453,305.62
2014	54,035,409.75	135,835,000.00	189,870,409.75
2015	48,038,653.05	118,735,000.00	166,773,653.05
2016	42,123,571.90	121,930,000.00	164,053,571.90
2017	35,895,849.29	129,925,000.00	165,820,849.29
2018	29,865,583.99	105,035,000.00	134,900,583.99
2019	24,519,579.11	100,850,000.00	125,369,579.11
2020	20,506,283.61	52,590,000.00	73,096,283.61
2021	17,704,637.50	45,615,000.00	63,319,637.50
2022	15,228,971.25	41,240,000.00	56,468,971.25
2023	13,480,617.01	21,730,000.00	35,210,617.01
2024	12,264,105.52	23,025,000.00	35,289,105.52
2025	10,949,341.91	25,350,000.00	36,299,341.91
2026	9,740,973.75	18,805,000.00	28,545,973.75
2027	8,650,135.00	20,645,000.00	29,295,135.00
2028	7,687,360.00	14,215,000.00	21,902,360.00
2029	6,741,760.00	19,955,000.00	26,696,760.00
2030	5,404,392.50	28,100,000.00	33,504,392.50
2031	3,892,867.50	25,920,000.00	29,812,867.50
2032	2,395,225.00	27,375,000.00	29,770,225.00
2033	812,977.50	28,930,000.00	29,742,977.50
Total	$ 1,233,497,764.00	$ 2,234,610,000.00	$ 3,468,107,764.00

(a) Includes scheduled mandatory sinking fund payments.
(b) Total represents the remaining debt service requirements from April 1, 2004 through June 30, 2004.

SOURCE: State of California, Office of the Treasurer.

SCHEDULE OF DEBT SERVICE REQUIREMENTS
FOR LEASE-PURCHASE DEBT
As of March 1, 2004

Fiscal Year Ending June 30	Current Debt		
	Interest	**Principal (a)**	**Total**
2004	$ 139,111,899.86	$ 68,365,000.00	$ 207,476,899.86 (b)
2005	360,898,044.05	353,394,507.20	714,292,551.25
2006	340,992,400.18	382,227,554.60	723,219,954.78
2007	326,839,245.59	335,618,920.44	662,458,166.03
2008	307,123,128.35	344,471,787.98	651,594,916.33
2009	293,821,550.44	366,922,732.44	660,744,282.88
2010	269,679,662.75	356,036,633.76	625,716,296.51
2011	240,215,388.93	369,250,000.00	609,465,388.93
2012	220,936,131.81	353,255,000.00	574,191,131.81
2013	202,426,896.45	362,740,000.00	565,166,896.45
2014	183,432,753.81	366,455,000.00	549,887,753.81
2015	163,742,807.52	385,845,000.00	549,587,807.52
2016	143,210,856.24	367,865,000.00	511,075,856.24
2017	123,189,311.84	373,680,000.00	496,869,311.84
2018	103,374,292.16	389,160,000.00	492,534,292.16
2019	83,225,999.33	348,360,000.00	431,585,999.33
2020	64,929,395.95	319,395,000.00	384,324,395.95
2021	49,548,835.74	253,900,000.00	303,448,835.74
2022	36,257,006.24	224,945,000.00	261,202,006.24
2023	26,167,926.62	171,090,000.00	197,257,926.62
2024	18,357,327.00	81,190,000.00	99,547,327.00
2025	14,135,430.00	85,410,000.00	99,545,430.00
2026	10,169,818.75	72,910,000.00	83,079,818.75
2027	6,414,873.75	76,625,000.00	83,039,873.75
2028	2,533,562.50	64,850,000.00	67,383,562.50
Total	$ 3,730,734,545.86	$ 6,873,962,136.42	$ 10,604,696,682.28

(a) Includes scheduled mandatory sinking fund payments.
(b) Total represents the remaining debt service requirements from April 1, 2004 through June 30, 2004.

SOURCE: State of California, Office of the Treasurer.

STATE PUBLIC WORKS BOARD AND OTHER LEASE-PURCHASE FINANCING OUTSTANDING ISSUES

March 1, 2004

Name of Issue		Outstanding
GENERAL FUND SUPPORTED ISSUES:		
State Public Works Board		
California Community Colleges	$	518,825,000
Department of the Youth Authority		16,975,000
Department of Corrections *		2,566,489,754
Energy Efficiency Program (Various State Agencies) (a)		74,770,000
The Regents of The University of California * (b)		1,136,987,382
Trustees of The California State University		581,445,000
Various State Office Buildings		1,109,830,000
Total State Public Works Board Issues	**$**	**6,005,322,136**
Total Other State Building Lease Purchase Issues(c)	**$**	**868,640,000**
Total General Fund Supported Issues	**$**	**6,873,962,136**
SPECIAL FUND SUPPORTED ISSUES:		
East Bay State Building Authority Certificates of Participation (State of California Department of Transportation) *	$	62,967,452
San Bernardino Joint Powers Financing Authority (State of California Department of Transportation)		53,465,000
San Francisco State Building Authority (State of California Department of General Services Lease) (d)		38,685,000
Total Special Fund Supported Issues	**$**	**155,117,452**
TOTAL	**$**	**7,029,079,589**

* Includes the initial value of capital appreciation bonds rather than the accreted value.

(a) This program is self-liquidating based on energy cost savings.

(b) The Regents' obligations to the State Public Works Board are payable from lawfully available funds of The Regents which are held in The Regents' treasury funds and are separate from the State General Fund. A portion of The Regents' annual budget is derived from General Fund appropriations.

(c) Includes $180,450,000 Sacramento City Financing Authority Lease Revenue Bonds State of California - Cal EPA Building, 1998 Series A, which are supported by lease rentals from the California Environmental Protection Agency; these rental payments are subject to annual appropriation by the State Legislature.

(d) The sole tenant is the California Public Utilities Commission.

SOURCE: State of California, Office of the Treasurer.

STATE AGENCY REVENUE BONDS
AND CONDUIT FINANCING
As of December 31, 2003

Issuing Agency		Outstanding[(a)(b)]
State Programs Financing:		
California State University	$	950,538,000
Department of Water Resources - Central Valley Project		2,351,095,000
Department of Water Resources - Power Supply Program		11,263,500,000
The Regents of the University of California		4,378,720,000
Housing Financing:		
California Housing Finance Agency		7,996,115,073
Veterans Revenue Debenture		503,200,000
Conduit Financing:		
California Alternative Energy and Advanced Transportation Financing Authority		58,860,000
California Educational Facilities Authority		3,023,765,116
California Health Facilities Financing Authority		6,559,319,243
California Infrastructure and Economic Development Bank [(c)]		3,263,607,962
California Pollution Control Financing Authority		3,946,659,157
California School Finance Authority		45,000
California Student Loan Authority		95,260,000
TOTAL	**$**	**44,390,684,551**

[(a)] Totals for California State University, Department of Water Resources-Central Valley Project, and Veterans Revenue Debenture were provided by the State of California, Office of the Treasurer. All other totals were provided by the listed issuing agency.

[(b)] Does not include $5.6 Billion of "tobacco settlement revenue bonds" issued by Golden State Tobacco Securitization Corporation.

[(c)] Does not include $6 billion of "rate reduction bonds" issued by special purpose trusts for the benefit of four investor-owned electric utility companies representing interests in certain electric rate surcharges.

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STATEMENT of GENERAL FUND CASH RECEIPTS and DISBURSEMENTS

February 2004

STEVE WESTLY
California State Controller

STEVE WESTLY

California State Controller

March 10, 2004

Users of the Statement of General Fund Cash Receipts and Disbursements

Attached are the Statements of General Fund Cash Receipts and Disbursements for the period July 1, 2003 through February 29, 2004. These statements reflect the State of California's General Fund cash position and compare actual receipts and disbursements for the 2003-04 fiscal year to cash flow estimates prepared by the Department of Finance for the 2004-05 Governor's Budget as well as the 2003-04 Budget Act. These statements are prepared in compliance with Government Code section 12461.1, as well as Item 0840-001-0001, Provision 10, of the 2003-04 Budget Act, using records compiled by the State Controller.

Attachment A compares actual receipts and disbursements to date for the 2003-04 fiscal year to cash flow estimates published in the 2004-05 Governor's Budget. <u>The Governor's Budget cash flow reflects an expected increase of $3.1 billion in receipts, and an expected increase of $4.9 billion in disbursements from the Budget Act estimate for the 2003-04 fiscal year. These cash flow estimates are predicated on projections and assumptions made by the Department of Finance in preparation of the Governor's Budget.</u>

Attachment B compares actual receipts and disbursements to date for the 2003-04 fiscal year to cash flow estimates prepared by the Department of Finance based upon the 2003-04 Budget Act. Prior year actual amounts are also displayed for comparative purposes.

These statements are also available on the Internet at the State Controller's website at **http://www.sco.ca.gov/ard/state/index.shtml** under the category Monthly Statement of General Fund Cash Receipts and Disbursements.

Any questions concerning this report may be directed to Vincent P. Brown, Chief Operating Officer, at (916) 552-8080.

Sincerely,

Steve Westly

STEVE WESTLY
California State Controller

300 Capitol Mall, Suite 1850, Sacramento, CA 95814 ♦ P.O. Box 942850, Sacramento, CA 94250
PHONE: (916) 445-2636 ♦ Fax: (916) 445-6379 ♦ Web Address: www.sco.ca.gov ♦ E-Mail: steve@sco.ca.gov

STATEMENT OF GENERAL FUND CASH RECEIPTS AND DISBURSEMENTS
A Comparison of Actual to 2004-05 Governor's Budget Estimates
(Amounts in thousands)
Attachment A

	July 1 through February 29				
	2004				2003 (a)
	Actual	Estimate (b)	Actual Over or (Under) Estimate Amount	%	Actual
GENERAL FUND BEGINNING CASH BALANCE	**$ 438,110**	**$ 438,110**	**$ -**	**-**	**$ -**
Add Receipts:					
Revenues	46,944,712	47,311,951	(367,239)	(0.8)	44,392,292
Nonrevenues	3,370,019	1,463,591	1,906,428	130.3	9,251,420
Total Receipts	50,314,731	48,775,542	1,539,189	3.2	53,643,712
Less Disbursements:					
State Operations	12,286,894	12,177,412	109,482	0.9	12,952,294 (a)
Local Assistance	44,032,164	43,526,945	505,219	1.2	42,585,690 (a)
Capital Outlay	208,977	148,490	60,487	40.7	123,573
Nongovernmental	1,980,697	(201,623)	2,182,320	-	40,231
Total Disbursements	58,508,732	55,651,224	2,857,508	5.1	55,701,788
Receipts Over / (Under) Disbursements	(8,194,001)	(6,875,682)	(1,318,319)	-	(2,058,076)
Net Increase / (Decrease) in Temporary Loans	7,755,891	6,437,572	1,318,319	20.5	2,058,813
GENERAL FUND ENDING CASH BALANCE	**-**	**-**	**-**	**-**	**737**
Special Fund for Economic Uncertainties	-	-	-	-	-
TOTAL CASH	**$ -**	**$ -**	**$ -**	**-**	**$ 737**

BORROWABLE RESOURCES					
Available Borrowable Resources	$ 24,096,927	$ 23,215,187	$ 881,740	3.8	$ 22,413,239
Outstanding Loans (c)	18,720,891	17,402,572	1,318,319	7.6	16,117,793 (a) (d)
Unused Borrowable Resources	$ 5,376,036	$ 5,812,615	$ (436,579)	(7.5)	$ 6,295,446

General Note:
This report is based upon funded cash. Funded cash is cash reported to and recorded in the records of the State Controller's Office. Amounts reported as funded cash may differ from amounts in other reports to the extent there are timing differences in the recording of in-transit items.

Footnotes:
(a) The General Cash Revolving Fund (GCRF) disbursements and loans have been combined with the General Fund for reporting purposes because they represent major General Fund type activities.
(b) A Statement of Estimated Cash Flow for the 2003-04 fiscal year prepared by the Department of Finance for the 2004-05 Governor's Budget. Any projections or estimates are set forth as such and not as representations of fact.
(c) Cumulative loan balance of $18.7 billion is comprised of $4.7 billion in internal borrowing and $14.0 billion in external borrowing.
(d) Cumulative loan balance of $16.1 billion is comprised of $3.6 billion in internal borrowing and $12.5 billion in external borrowing of which $3.6 billion remains in the Special Deposit Revenue Anticipation Notes Proceeds Account.
(e) Negative balances are the result of repayments received that are greater than disbursements made.
(f) Reclassified from a Non-Governmental Cost Fund.

SCHEDULE OF CASH RECEIPTS
(Amounts in thousands)

	Month of February		July 1 through February 29				
			2004				2003 (a)
	2004	2003	Actual	Estimate (b)	Actual Over or (Under) Estimate Amount	%	Actual
REVENUES							
Alcoholic Beverage Excise Tax	$ 18,969	$ 19,825	$ 214,495	$ 207,265	$ 7,230	3.5	$ 200,239
Corporation Tax	113,563	171,130	3,271,625	3,268,320	3,305	0.1	2,730,070
Cigarette Tax	7,835	11,062	75,881	76,133	(252)	(0.3)	87,345
Estate, Inheritance, and Gift Tax	29,869	90,669	394,742	391,335	3,407	0.9	633,704
Insurance Companies Tax	15,813	14,672	934,587	936,302	(1,715)	(0.2)	810,461
Personal Income Tax	1,412,540	1,291,270	23,175,875	23,484,003	(308,128)	(1.3)	21,282,913
Retail Sales and Use Taxes	3,303,428	3,105,774	15,510,086	15,407,273	102,813	0.7	14,804,178
Pooled Money Investment Interest	10,145	20,394	78,396	90,926	(12,530)	(13.8)	136,923
Not Otherwise Classified	109,845	47,944	3,289,025	3,450,394	(161,369)	(4.7)	3,706,459
Total Revenues	**5,022,007**	**4,772,740**	**46,944,712**	**47,311,951**	**(367,239)**	**(0.8)**	**44,392,292**
NONREVENUES							
Transfers from Special Fund for Economic Uncertainties	2,524,497	-	2,524,497	308,219	2,216,278	719.1	-
Transfers from Other Funds	55,538	58,776	493,597	839,493	(345,896)	(41.2)	2,750,005
Transfers from Electric Power Fund	-	-	-	-	-	-	6,094,067
Miscellaneous	119,415	156,883	351,925	315,879	36,046	11.4	407,348
Total Nonrevenues	**2,699,450**	**215,659**	**3,370,019**	**1,463,591**	**1,906,428**	**130.3**	**9,251,420**
Total Receipts	**$ 7,721,457**	**$ 4,988,399**	**$ 50,314,731**	**$ 48,775,542**	**$ 1,539,189**	**3.2**	**$ 53,643,712**

See notes on page 1.

SCHEDULE OF CASH DISBURSEMENTS
(Amounts in thousands)

	Month of February		July 1 through February 29				
			2004				2003 (a)
	2004	2003	Actual	Estimate (b)	Actual Over or (Under) Estimate Amount	%	Actual
STATE OPERATIONS (e)							
Legislative/Judicial/Executive	$ 89,071	$ 111,129	$ 915,604	$ 900,367	$ 15,237	1.7	$ 921,845
State and Consumer Services	35,988	40,648	324,691	316,851	7,840	2.5	303,354
Business, Transportation and Housing	334	1,262	6,258	6,259	(1)	-	6,869
Technology, Trade and Commerce	107	2,149	6,983	5,148	1,835	35.6	15,676
Resources	57,793	55,068	632,562	649,084	(16,522)	(2.5)	696,212
Environmental Protection Agency	5,989	4,119	58,927	63,023	(4,096)	(6.5)	106,129
Health and Human Services:							
Health Services	41,926	11,273	224,458	244,834	(20,376)	(8.3)	206,863
Mental Health Hospitals	34,932	47,049	389,953	412,422	(22,469)	(5.4)	402,052
Other Health and Human Services	45,015	37,306	509,383	483,998	25,385	5.2	440,521
Education:							
University of California	274,911	307,478	2,305,566	2,188,188	117,378	5.4	2,354,064 (a)
State Universities and Colleges	179,766	115,592	1,705,496	1,704,055	1,441	0.1	1,781,238
Other Education	8,378	14,089	109,928	109,645	283	0.3	131,141
Corrections and Youth Authority	461,417	442,205	3,134,375	3,065,243	69,132	2.3	3,712,626
General Government	88,127	100,898	802,133	774,000	28,133	3.6	808,222
Public Employees Retirement System	(116,005)	(67,334)	(29,647)	(35,410)	5,763	-	(11,194)
Debt Service	283,516	169,210	1,200,927	1,202,802	(1,875)	(0.2)	995,801
Interest on Loans	-	10,181	(10,703)	86,903	(97,606)	(112.3)	80,875
Total State Operations	**1,491,265**	**1,402,322**	**12,286,894**	**12,177,412**	**109,482**	**0.9**	**12,952,294**
LOCAL ASSISTANCE (e)							
Public Schools - K-12	4,075,464	3,705,910	20,259,466	20,322,490	(63,024)	(0.3)	17,984,637 (a)
Community Colleges	248,360	252,173	1,644,613	1,588,333	56,280	3.5	1,917,377 (a)
Contributions to State Teachers' Retirement System	-	-	397,039	397,039	-	-	867,887
Other Education	156,762	122,752	1,987,743	1,735,836	251,907	14.5	1,854,376
Corrections and Youth Authority	27,778	20,612	108,303	108,018	285	0.3	117,842
Dept. of Alcohol and Drug Program	9,617	8,587	177,734	188,781	(11,047)	(5.9)	196,342
Dept. of Health Services:							
Medical Assistance Program	928,172	784,275	7,144,997	6,788,479	356,518	5.3	7,039,600
Other Health Services	43,823	63,573	276,525	279,736	(3,211)	(1.1)	327,241
Dept. of Developmental Services	81,909	(15,725)	1,289,501	1,141,932	147,569	12.9	1,064,822
Dept. of Mental Health	(91,582)	8,266	326,118	451,952	(125,834)	(27.8)	430,061
Dept. of Social Services:							
SSI/SSP/IHSS	464,401	309,411	3,819,747	3,817,707	2,040	0.1	2,962,490
CalWORKs	113,757	105,694	2,323,932	2,293,089	30,843	1.3	2,030,721
Other Social Services	76,951	114,676	776,657	758,795	17,862	2.4	918,409
Tax Relief	333,400	296,572	1,515,198	1,604,305	(89,107)	(5.6)	2,961,347
School Facility Aid Program	13,953	-	13,953	-	13,953	-	15,566
Other Local Assistance	270,403	154,678	1,970,638	2,050,453	(79,815)	(3.9)	1,896,972
Total Local Assistance	**6,753,168**	**5,931,454**	**44,032,164**	**43,526,945**	**505,219**	**1.2**	**42,585,690**

See notes on page 1.

(Continued)

SCHEDULE OF CASH DISBURSEMENTS (Continued)
(Amounts in thousands)

	Month of February		July 1 through February 29				
			2004				2003 (a)
	2004	2003	Actual	Estimate (b)	Actual Over or (Under) Estimate Amount	%	Actual
CAPITAL OUTLAY	**75,299**	**17,300**	**208,977**	**148,490**	**60,487**	**40.7**	**123,573**
NONGOVERNMENTAL (e)							
Transfer to Special Fund for Economic Uncertainties	2,216,000	-	2,216,000	-	2,216,000	-	-
Transfer to Other Funds	7,980	50	245,119	270,090	(24,971)	(9.2)	71,680
Transfer to Revolving Fund	677	21,688	2,887	(2,637)	5,524	-	82,641
Advance:							
State-County Property Tax Administration Program	-	-	-	-	-	-	9,677
Social Welfare Federal Fund	(45,326)	18,770	(6,850)	11,383	(18,233)	(160.2)	121,677
Tax Relief and Refund Account	4,000	(200)	4,000	-	4,000	-	2,400
Counties for Social Welfare	-	-	(480,459)	(480,459)	-	-	(247,844)
Total Nongovernmental	**2,183,331**	**40,308**	**1,980,697**	**(201,623)**	**2,182,320**	**-**	**40,231**
Total Disbursements	**10,503,063**	**$ 7,391,384**	**$ 58,508,732**	**$ 55,651,224**	**$ 2,857,508**	**5.1**	**$ 55,701,788**
TEMPORARY LOANS							
Special Fund for Economic Uncertainties	241,738	$ 2,524,519	$ 2,216,023	$ 2,216,300	$ (277)	-	$ -
Other Internal Sources	2,539,868	1,093,274	2,539,868	1,221,272	1,318,596	108.0	669,813
Revenue Anticipation Warrants	-	-	-	-	-	-	(7,500,000)
Revenue Anticipation Notes	-	(3,611,000) (d)	3,000,000	3,000,000	-	-	8,889,000
Net Increase / (Decrease) Loans	**2,781,606**	**$ 6,793**	**$ 7,755,891**	**$ 6,437,572**	**$ 1,318,319**	**20.5**	**$ 2,058,813**

See notes on page 1.

(Concluded)

COMPARATIVE STATEMENT OF REVENUES RECEIVED
All Governmental Cost Funds
(Amounts in thousands)

	July 1 through February 29			
	General Fund		Special Funds	
	2004	2003	2004	2003
MAJOR TAXES, LICENSES, AND INVESTMENT INCOME:				
Alcoholic Beverage Excise Taxes	$ 214,495	$ 200,239	$ -	$ -
Corporation Tax	3,271,625	2,730,070	9	7
Cigarette Tax	75,881	87,345	618,153	699,379
Estate, Inheritance, and Gift Tax	394,742	633,704	-	-
Insurance Companies Tax	934,587	810,461	-	-
Motor Vehicle Fuel Tax:				
Gasoline Tax	-	-	1,888,928	1,880,365
Diesel & Liquid Petroleum Gas	-	-	346,269	323,972
Jet Fuel Tax	-	-	1,243	1,640
Vehicle License Fees	-	-	1,636,202	1,253,683
Motor Vehicle Registration and Other Fees	-	-	1,477,936	1,305,996
Personal Income Tax	23,175,875	21,282,913	213	242
Retail Sales and Use Taxes	15,510,086	14,804,178	3,276,384	3,160,909
Pooled Money Investment Interest	78,396	136,923	90	381
Total Major Taxes, Licenses, and Investment Income	**43,655,687**	**40,685,833**	**9,245,427**	**8,626,574**
NOT OTHERWISE CLASSIFIED:				
Alcoholic Beverage License Fee	1,541	1,765	27,723	23,023
Electrical Energy Tax	-	-	316,221	330,494
Private Rail Car Tax	6,636	6,340	-	-
Penalties on Traffic Violations	-	-	48,785	49,253
Health Care Receipts	9,614	4,775	-	-
Revenues from State Lands	54,525	27,387	7,904	9,218
Abandoned Property	486,762	237,381	-	-
Trial Court Revenues	26,910	173	623,593 (f)	-
Horse Racing Fees	1,547	2,623	24,192	24,668
Miscellaneous	2,701,490	3,426,015	4,137,390	3,809,081
Not Otherwise Classified	**3,289,025**	**3,706,459**	**5,185,808**	**4,245,737**
Total Revenues, All Governmental Cost Funds	**$ 46,944,712**	**$ 44,392,292**	**$ 14,431,235**	**$ 12,872,311**

See notes on page 1.

STATEMENT OF GENERAL FUND CASH RECEIPTS AND DISBURSEMENTS
A Comparison of Actual to 2003-04 Budget Act Estimates
(Amounts in thousands)
Attachment B

	July 1 through February 29				
	2004				2003 (a)
	Actual	Estimate (b)	Actual Over or (Under) Estimate Amount	%	Actual
GENERAL FUND BEGINNING CASH BALANCE	**$ 438,110**	**$ 438,110**	**$ -**	**-**	**$ -**
Add Receipts:					
Revenues	46,944,712	51,000,859	(4,056,147)	(8.0)	44,392,292
Nonrevenues	3,370,019	1,318,376	2,051,643	155.6	9,251,420
Total Receipts	50,314,731	52,319,235	(2,004,504)	(3.8)	53,643,712
Less Disbursements:					
State Operations	12,286,894	12,115,645	171,249	1.4	12,952,294 (a)
Local Assistance	44,032,164	41,890,875	2,141,289	5.1	42,585,690 (a)
Capital Outlay	208,977	49,283	159,694	324.0	123,573
Nongovernmental	1,980,697	119,744	1,860,953	1,554.1	40,231
Total Disbursements	58,508,732	54,175,547	4,333,185	8.0	55,701,788
Receipts Over / (Under) Disbursements	(8,194,001)	(1,856,312)	(6,337,689)	-	(2,058,076)
Net Increase / (Decrease) in Temporary Loans	7,755,891	3,000,000	4,755,891	158.5	2,058,813
GENERAL FUND ENDING CASH BALANCE	**-**	**1,581,798**	**(1,581,798)**	**(100.0)**	**737**
Special Fund for Economic Uncertainties	-	2,216,300	(2,216,300)	(100.0)	-
TOTAL CASH	**$ -**	**$ 3,798,098**	**$ (3,798,098)**	**(100.0)**	**$ 737**

	Actual	Estimate (b)	Amount	%	2003 (a) Actual
BORROWABLE RESOURCES					
Available Borrowable Resources	$ 24,096,927	$ 23,273,213	$ 823,714	3.5	$ 22,413,239
Outstanding Loans (c)	18,720,891	13,965,000	4,755,891	34.1	16,117,793 (a) (d)
Unused Borrowable Resources	$ 5,376,036	$ 9,308,213	$ (3,932,177)	(42.2)	$ 6,295,446

General Note:
This report is based upon funded cash. Funded cash is cash reported to and recorded in the records of the State Controller's Office. Amounts reported as funded cash may differ from amounts in other reports to the extent there are timing differences in the recording of in-transit items.

Footnotes:
(a) The General Cash Revolving Fund (GCRF) disbursements and loans have been combined with the General Fund for reporting purposes because they represent major General Fund type activities.
(b) A Statement of Estimated Cash Flow for the 2003-04 fiscal year prepared by the Department of Finance for the Budget Act of 2003. Any projections or estimates are set forth as such and not as representations of fact.
(c) Cumulative loan balance of $18.7 billion is comprised of $4.7 billion in internal borrowing and $14.0 billion in external borrowing.
(d) Cumulative loan balance of $16.1 billion is comprised of $3.6 billion in internal borrowing and $12.5 billion in external borrowing of which $3.6 billion remains in the Special Deposit Revenue Anticipation Notes Proceeds Account.
(e) Negative balances are the result of repayments received that are greater than disbursements made.

SCHEDULE OF CASH RECEIPTS
(Amounts in thousands)

	Month of February		July 1 through February 29				
			2004				2003 (a)
					Actual Over or (Under) Estimate		
	2004	2003	Actual	Estimate (b)	Amount	%	Actual
REVENUES							
Alcoholic Beverage Excise Tax	$ 18,969	$ 19,825	$ 214,495	$ 202,070	$ 12,425	6.1	$ 200,239
Corporation Tax	113,563	171,130	3,271,625	2,981,030	290,595	9.7	2,730,070
Cigarette Tax	7,835	11,062	75,881	77,452	(1,571)	(2.0)	87,345
Estate, Inheritance, and Gift Tax	29,869	90,669	394,742	436,763	(42,021)	(9.6)	633,704
Insurance Companies Tax	15,813	14,672	934,587	930,219	4,368	0.5	810,461
Personal Income Tax	1,412,540	1,291,270	23,175,875	22,378,968	796,907	3.6	21,282,913
Retail Sales and Use Taxes	3,303,428	3,105,774	15,510,086	15,344,649	165,437	1.1	14,804,178
Pooled Money Investment Interest	10,145	20,394	78,396	137,137	(58,741)	(42.8)	136,923
Not Otherwise Classified	109,845	47,944	3,289,025	3,174,871	114,154	3.6	3,706,459
Deficit Financing Bond Proceeds	-	-	-	5,337,700	(5,337,700)	(100.0)	-
Total Revenues	**5,022,007**	**4,772,740**	**46,944,712**	**51,000,859**	**(4,056,147)**	**(8.0)**	**44,392,292**
NONREVENUES							
Transfers from Special Fund for Economic Uncertainties	2,524,497	-	2,524,497	308,219	2,216,278	719.1	-
Transfers from Other Funds	55,538	58,776	493,597	710,775	(217,178)	(30.6)	2,750,005
Transfers from Electric Power Fund	-	-	-	-	-	-	6,094,067
Miscellaneous	119,415	156,883	351,925	299,382	52,543	17.6	407,348
Total Nonrevenues	**2,699,450**	**215,659**	**3,370,019**	**1,318,376**	**2,051,643**	**155.6**	**9,251,420**
Total Receipts	**$ 7,721,457**	**$ 4,988,399**	**$ 50,314,731**	**$ 52,319,235**	**$ (2,004,504)**	**(3.8)**	**$ 53,643,712**

See notes on page 1.

SCHEDULE OF CASH DISBURSEMENTS
(Amounts in thousands)

	Month of February		July 1 through February 29				
			2004				2003 (a)
	2004	2003	Actual	Estimate (b)	Actual Over or (Under) Estimate Amount	%	Actual
STATE OPERATIONS (e)							
Legislative/Judicial/Executive	$ 89,071	$ 111,129	$ 915,604	$ 764,808	$ 150,796	19.7	$ 921,845
State and Consumer Services	35,988	40,648	324,691	291,191	33,500	11.5	303,354
Business, Transportation and Housing	334	1,262	6,258	5,798	460	7.9	6,869
Technology, Trade and Commerce	107	2,149	6,983	5,343	1,640	30.7	15,676
Resources	57,793	55,068	632,562	534,617	97,945	18.3	696,212
Environmental Protection Agency	5,989	4,119	58,927	64,528	(5,601)	(8.7)	106,129
Health and Human Services:							
Health Services	41,926	11,273	224,458	211,695	12,763	6.0	206,863
Mental Health Hospitals	34,932	47,049	389,953	412,044	(22,091)	(5.4)	402,052
Other Health and Human Services	45,015	37,306	509,383	421,963	87,420	20.7	440,521
Education:							
University of California	274,911	307,478	2,305,566	2,070,339	235,227	11.4	2,354,064 (a)
State Universities and Colleges	179,766	115,592	1,705,496	1,747,304	(41,808)	(2.4)	1,781,238
Other Education	8,378	14,089	109,928	104,425	5,503	5.3	131,141
Corrections and Youth Authority	461,417	442,205	3,134,375	3,511,238	(376,863)	(10.7)	3,712,626
General Government	88,127	100,898	802,133	251,507	550,626	218.9	808,222
Public Employees Retirement System	(116,005)	(67,334)	(29,647)	438,920	(468,567)	(106.8)	(11,194)
Debt Service	283,516	169,210	1,200,927	1,210,403	(9,476)	(0.8)	995,801
Interest on Loans	-	10,181	(10,703)	69,522	(80,225)	(115.4)	80,875
Total State Operations	**1,491,265**	**1,402,322**	**12,286,894**	**12,115,645**	**171,249**	**1.4**	**12,952,294**
LOCAL ASSISTANCE (e)							
Public Schools - K-12	4,075,464	3,705,910	20,259,466	19,867,217	392,249	2.0	17,984,637 (a)
Community Colleges	248,360	252,173	1,644,613	1,573,973	70,640	4.5	1,917,377 (a)
Contributions to State Teachers' Retirement System	-	-	397,039	397,040	(1)	-	867,887
Other Education	156,762	122,752	1,987,743	1,675,501	312,242	18.6	1,854,376
Corrections and Youth Authority	27,778	20,612	108,303	125,566	(17,263)	(13.7)	117,842
Dept. of Alcohol and Drug Program	9,617	8,587	177,734	321,667	(143,933)	(44.7)	196,342
Dept. of Health Services:							
Medical Assistance Program	928,172	784,275	7,144,997	7,683,775	(538,778)	(7.0)	7,039,600
Other Health Services	43,823	63,573	276,525	269,808	6,717	2.5	327,241
Dept. of Developmental Services	81,909	(15,725)	1,289,501	1,586,613	(297,112)	(18.7)	1,064,822
Dept. of Mental Health	(91,582)	8,266	326,118	407,530	(81,412)	(20.0)	430,061
Dept. of Social Services:							
SSI/SSP/IHSS	464,401	309,411	3,819,747	3,476,934	342,813	9.9	2,962,490
CalWORKs	113,757	105,694	2,323,932	2,088,987	234,945	11.2	2,030,721
Other Social Services	76,951	114,676	776,657	911,347	(134,690)	(14.8)	918,409
Tax Relief	333,400	296,572	1,515,198	361,837	1,153,361	318.8	2,961,347
School Facility Aid Program	13,953	-	13,953	11,851	2,102	17.7	15,566
Other Local Assistance	270,403	154,678	1,970,638	1,131,229	839,409	74.2	1,896,972
Total Local Assistance	**6,753,168**	**5,931,454**	**44,032,164**	**41,890,875**	**2,141,289**	**5.1**	**42,585,690**

See notes on page 1.

(Continued)

SCHEDULE OF CASH DISBURSEMENTS (Continued)
(Amounts in thousands)

	Month of February		July 1 through February 29				
			2004				2003 (a)
	2004	2003	Actual	Estimate (b)	Actual Over or (Under) Estimate Amount	%	Actual
CAPITAL OUTLAY	**75,299**	**17,300**	**208,977**	**49,283**	**159,694**	**324.0**	**123,573**
NONGOVERNMENTAL (e)							
Transfer to Special Fund for Economic Uncertainties	2,216,000	-	2,216,000	-	2,216,000	-	-
Transfer to Other Funds	7,980	50	245,119	232,384	12,735	5.5	71,680
Transfer to Revolving Fund	677	21,688	2,887	(10,328)	13,215	-	82,641
Advance:							
State-County Property Tax Administration Program	-	-	-	-	-	-	9,677
Social Welfare Federal Fund	(45,326)	18,770	(6,850)	(102,312)	95,462	-	121,677
Tax Relief and Refund Account	4,000	(200)	4,000	-	4,000	-	2,400
Counties for Social Welfare	-	-	(480,459)	-	(480,459)	-	(247,844)
Total Nongovernmental	**2,183,331**	**40,308**	**1,980,697**	**119,744**	**1,860,953**	**1,554.1**	**40,231**
Total Disbursements	**10,503,063**	**$ 7,391,384**	**$ 58,508,732**	**$ 54,175,547**	**$ 4,333,185**	**8.0**	**$ 55,701,788**
TEMPORARY LOANS							
Special Fund for Economic Uncertainties	241,738	$ 2,524,519	$ 2,216,023	$ -	$ 2,216,023	-	$ - (a)
Other Internal Sources	2,539,868	1,093,274	2,539,868	-	2,539,868	-	669,813 (a)
Revenue Anticipation Warrants	-	-	-	-	-	-	(7,500,000)
Revenue Anticipation Notes	-	(3,611,000) (d)	3,000,000	3,000,000	-	-	8,889,000
Net Increase / (Decrease) Loans	**2,781,606**	**$ 6,793**	**$ 7,755,891**	**$ 3,000,000**	**$ 4,755,891**	**158.5**	**$ 2,058,813**

See notes on page 1.

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APPENDIX B

DTC AND THE BOOK-ENTRY SYSTEM

THE INFORMATION IN THIS APPENDIX CONCERNING THE DEPOSITORY TRUST COMPANY, NEW YORK, NEW YORK ("DTC") AND DTC'S BOOK-ENTRY SYSTEM HAS BEEN OBTAINED FROM SOURCES THAT THE TREASURER OF THE STATE OF CALIFORNIA ("STATE TREASURER") BELIEVES TO BE RELIABLE, BUT THE STATE TREASURER, THE FINANCIAL ADVISOR AND THE UNDERWRITERS TAKE NO RESPONSIBILITY FOR THE ACCURACY THEREOF.

The Depository Trust Company ("DTC"), New York, New York, will act as securities depository for the bonds (the "Bonds"). The Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Bond certificate will be issued for each maturity of the Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

DTC is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934, as amended. DTC holds and provides asset servicing for over 2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation, ("NSCC," "GSCC," "MBSCC" and "EMCC," also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

Purchases of Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC's records. The ownership interest of each actual purchaser of each Bond ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmation providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Bonds, except in the event that use of the book-entry system for the Bonds is discontinued.

To facilitate subsequent transfers, all Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds: DTC's records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. The State Treasurer will not have any responsibility or obligation to such Direct Participants and Indirect Participants or the persons for whom they act as nominees with respect to the Bonds. Beneficial Owners of Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Bonds, such as redemptions, tenders, defaults, and proposed amendments to the Bond documents. Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

Redemption notices will be sent to DTC. If less than all of the Bonds within a maturity are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the State Treasurer as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and interest payments on the Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the State Treasurer, on payable dates in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC nor its nominee, or the State Treasurer, subject to any statutory, or regulatory requirements as may be in effect from time to time. Payment of principal and interest to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the State Treasurer, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

If the State Treasurer determines not to continue the DTC book-entry only system, or DTC discontinues providing its services with respect to the Bonds and the State Treasurer does not select another qualified securities depository, the State will deliver physical Bond certificates to the beneficial owners. The Bonds may thereafter be transferred upon the books of the State Treasurer by the registered owners, in person or by authorized attorney, upon surrender of Bonds at the Office of the State Treasurer in Sacramento, California, accompanied by delivery of an executed instrument of transfer in a form approved by the State Treasurer and upon payment of any charges provided for in the Resolution.

Certificated bonds may be exchanged for Bonds of other authorized denominations of the same aggregate principal amount and maturity at the Office of the State Treasurer in Sacramento, California, upon payment of any charges provided for in the Resolution. No transfer or exchange of Bonds will be made by the State Treasurer during the period between the record date and the next Interest Payment Date.

THE STATE TREASURER, AS LONG AS A BOOK-ENTRY ONLY SYSTEM IS USED FOR THE BONDS, WILL SEND ANY NOTICE OF REDEMPTION OR OTHER NOTICES TO OWNERS TO ONLY DTC. ANY FAILURE OF DTC TO ADVISE ANY DTC PARTICIPANT, OR OF ANY DTC PARTICIPANT TO NOTIFY ANY BENEFICIAL OWNER, OF ANY NOTICE AND ITS CONTENT OR EFFECT WILL NOT AFFECT THE VALIDITY OR SUFFICIENCY OF THE PROCEEDINGS RELATING TO THE REDEMPTION OF THE BONDS CALLED FOR REDEMPTION OR OF ANY OTHER ACTION PREMISED ON SUCH NOTICE.

Neither the State Treasurer nor the Underwriters can and does give any assurances that DTC will distribute to Participants, or that Participants or others will distribute to the Beneficial Owners, payment of principal of and interest on the Bonds paid or any redemption or other notices or that they will do so on a timely basis or will serve and act in the manner described in this Official Statement. Neither the State Treasurer nor the Underwriters is responsible or liable for the failure of DTC or any Direct Participant or Indirect Participant to make any payments or give any notice to a Beneficial Owner with respect to the Bonds or any error or delay relating thereto.

The foregoing description of the procedures and record keeping with respect to beneficial ownership interests in the Bonds, payment of principal of and interest and other payments with respect to the Bonds to Direct Participants, Indirect Participants or Beneficial Owners, confirmation and transfer of beneficial ownership interest in such Bonds and other related transactions by and between DTC, the Direct Participants, the Indirect Participants and the Beneficial Owners is based solely on information provided by DTC. Accordingly, no representations can be made concerning these matters and neither the Direct Participants, the Indirect Participants not the Beneficial Owners should rely on the foregoing information with respect to such matters but should instead confirm the same with DTC or the Participants, as the case may be.

SO LONG AS CEDE & CO. IS THE REGISTERED OWNER OF THE BONDS, AS NOMINEE OF DTC, REFERENCES HEREIN TO THE HOLDERS OF THE BONDS (OTHER THAN UNDER THE CAPTION “TAX MATTERS” HEREIN) SHALL MEAN CEDE & CO., AS AFORESAID, AND SHALL NOT MEAN THE BENEFICIAL OWNERS OF THE BONDS.

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APPENDIX C

FORM OF CONTINUING DISCLOSURE CERTIFICATE

This Continuing Disclosure Certificate (this "Disclosure Certificate") is executed as of April __, 2004, by the Treasurer of the State of California (the "State Treasurer") in connection with the issuance of $_______ aggregate principal amount of the State of California Various Purpose General Obligation Bonds (the "Bonds") as authorized by various acts of the State of California legislature (the "Acts"). The Bonds are being issued pursuant to resolutions of finance committees (the "Resolutions"), created under the Acts. Pursuant to the Resolutions, the State Treasurer, on behalf of the State of California (the "State"), covenants and agrees as follows:

SECTION 1. Nature of the Disclosure Certificate. This Disclosure Certificate is executed for the benefit of the Holders and Beneficial Owners (as defined below) of the Bonds from time to time, and in order to assist the Participating Underwriters (as defined below) in complying with the Rule, but shall not be deemed to create any monetary liability on the part of the State or the State Treasurer to any other persons, including Holders or Beneficial Owners of the Bonds based on the Rule (as defined below). The sole remedy in the event of any failure of the State Treasurer to comply with this Disclosure Certificate shall be an action to compel performance of any act required hereunder.

SECTION 2. Definitions. In addition to the definitions set forth in the Resolution, which apply to any capitalized term used in this Disclosure Certificate unless otherwise defined in this Section, the following capitalized terms shall have the following meanings:

"Annual Report" shall mean the Annual Report filed by the State Treasurer pursuant to, and as described in, Sections 3 and 4 of this Disclosure Certificate.

"Beneficial Owner" shall mean any person who has or shares the power, directly or indirectly, to make investment decisions concerning ownership of any Bonds (including persons holding Bonds through nominees, depositories or other intermediaries).

"Dissemination Agent" shall mean the State Treasurer, acting in its capacity as Dissemination Agent hereunder, or any successor Dissemination Agent designated in writing by the State Treasurer.

"Holder" shall mean any person listed on the registration books of the State Treasurer as the registered owner of any Bonds.

"Listed Event" shall mean any of the events listed in Section 5(a) of this Disclosure Certificate.

"National Repository" shall mean any Nationally Recognized Municipal Securities Information Repository certified by the Securities and Exchange Commission to be the recipient of information of the nature of the Annual Reports required by this Disclosure Certificate.

"Official Statement" shall mean the official statement relating to the Bonds, dated April __, 2004.

"Participating Underwriter" shall mean any original underwriters of the Bonds required to comply with the Rule in connection with the offering of the Bonds.

"Repository" shall mean each National Repository and the State Repository, if any.

"Rule" shall mean Rule 15c2-12(b)(5) adopted by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as the same may be amended from time to time.

"State" shall mean the State of California.

"State Repository" shall mean any public or private repository or entity within the State created for the purpose of receiving information of the nature of the reports of material events required by this Disclosure Certificate and recognized as such by the Securities and Exchange Commission (the "S.E.C."). As of the date of this Disclosure Certificate, there is no State Repository.

SECTION 3. Provision of Annual Reports.

(a) The State Treasurer on behalf of the State shall, not later than April 1 of each year in which the Bonds are outstanding, commencing with the report containing 2003-2004 Fiscal Year financial information, provide an Annual Report consistent with the requirements of the Disclosure Certificate (an "Annual Report") to each Repository; provided that the audited financial statements of the State may be submitted separately from the balance of the Annual Report and later than the date required above for the filing of the Annual Report if they are not available by that date. The State Treasurer shall make a copy of any Annual Report available to any person who requests a copy at a cost not exceeding the reasonable cost of duplication and delivery.

(b) If in any year, the State Treasurer does not provide the Annual Report to each Repository by the time specified above, the State Treasurer shall instead file a notice with each Repository stating that the Annual Report has not been timely completed and, if known, stating the date by which the State Treasurer expects to file the Annual Report.

(c) If the Dissemination Agent is not the State Treasurer, the Dissemination Agent shall:

1. determine each year prior to the date for filing the Annual Report the name and address of each Repository then certified by the S.E.C.;

2. file a report with the State Treasurer certifying that the Annual Report has been filed pursuant to this Disclosure Certificate and listing all the Repositories with which it was filed and the dates of the filings; and

3. take any other actions mutually agreed to between the Dissemination Agent and the State Treasurer.

SECTION 4. Content of Annual Reports. The Annual Report shall contain or include by reference the following:

(1) The audited General Purpose Financial Statements of the State for the fiscal year ended on the previous June 30, prepared in accordance with generally accepted accounting principles promulgated to apply to government entities from time to time by the Governmental Accounting Standards Board. If the State's audited financial statements are not available by the time the Annual Report is required to be filed pursuant to the Disclosure Certificate, the Annual Report shall contain unaudited financial statements in a format similar to the financial statements contained in the final Official Statement, and the audited financial statements shall be filed in the same manner as the Annual Report when they become available.

(2) Financial information relating to the State's General Fund budget for the fiscal year ended on the previous June 30 and information concerning the State budget for the fiscal year in which the Annual Report is issued. Such information shall describe the sources of revenues, the principal categories of expenditures, and changes in fund balances, a summary of expected State revenues and budgeted expenditures, and significant assumptions relating to revenue and expenditure expectations; including updating the following tables which appear under the caption "APPENDIX A – THE STATE OF CALIFORNIA – CURRENT STATE BUDGET" in the Official Statement:

<u>Table Entitled</u>

Statement of Revenues, Expenditures, and Changes in Fund Balance – General Fund

Revenue and Expenditure Assumptions

(3) Information concerning the total amount of the State's authorized and outstanding debt, long-term lease obligations and other long-term liabilities as of the end of the most recent June 30, which debt is supported by payments from the State's General Fund and which includes short-term debt. Such information shall include schedules of debt service for outstanding general obligation bonds and lease-purchase debt. This shall be accomplished by updating the following tables which appear under the caption "APPENDIX A – THE STATE OF CALIFORNIA – STATE DEBT TABLES" in the Official Statement.

<u>Table Entitled</u>

Authorized and Outstanding General
Obligation Bonds

Outstanding State Debt

Schedule of Debt Service Requirements for
General Fund General Obligation Bonds

Schedule of Debt Service Requirements for
Enterprise Fund General Obligation Bonds

Schedule of Debt Service Requirements for
Lease-Purchase Debt

State Public Works Board and
Other Lease-Purchase Financing Outstanding Issues

State Agency Revenue Bonds and
Conduit Financing

(4) Information concerning the State's actual cash flow results for the prior fiscal year. This shall be accomplished by providing a table showing actual cash flows for the preceding fiscal year similar to the tables which appear under the caption "APPENDIX A – THE STATE OF CALIFORNIA - CASH FLOW" in the Official Statement.

The Annual Report may consist of one or more documents. Any or all of the items listed above may be included in the Annual Report by reference to other documents that have been filed by the State with each of the Repositories, including any final official statement (in which case such final official statement must also be available from the Municipal Securities Rulemaking Board). The State Treasurer shall clearly identify in the Annual Report each such document so included by reference.

SECTION 5. Reporting of Significant Events.

(a) Pursuant to the provisions of this Section 5, the State Treasurer, on behalf of the State, shall give, or cause to be given, prompt notice of the occurrence of any of the following events with respect to the Bonds, if material:

1. principal and interest payment delinquencies;
2. non-payment related defaults;
3. modifications to rights of Holders;
4. optional, contingent or unscheduled bond calls;
5. defeasances;
6. rating changes;
7. adverse tax opinions or events affecting the tax-exempt status of the Bonds;
8. unscheduled draws on debt service reserves reflecting financial difficulties;
9. unscheduled draws on credit enhancements reflecting financial difficulties;
10. substitution of credit or liquidity providers, or their failure to perform; or
11. release, substitution or sale of property securing repayment of the Bonds.

The State Treasurer notes that items 8 through 11 above are not applicable to the Bonds.

(b) The State Treasurer shall timely file a notice of the occurrence of a Listed Event, which is material under applicable federal securities laws, with the Municipal Securities Rulemaking Board and each Repository.

SECTION 6. Termination of Reporting Obligation. The State's obligations under Section 3, 4 and 5 of this Disclosure Certificate shall terminate upon the maturity, legal defeasance, prior redemption or acceleration of all of the outstanding Bonds. If such termination occurs prior to the final maturity of the Bonds, the State Treasurer shall give notice of such termination in the same manner as for a Listed Event under Section 5(b).

SECTION 7. Dissemination Agent. The State Treasurer may, from time to time, appoint or engage a Dissemination Agent to assist it in carrying out the obligations under this Disclosure Certificate, and may discharge any such Dissemination Agent, with or without appointing a successor Dissemination Agent. The Dissemination Agent shall not be responsible in any manner for the content of any notice or report prepared by the State Treasurer pursuant to this Disclosure Certificate. If at any time there is not any other designated Dissemination Agent, the State Treasurer shall be the Dissemination Agent. The initial Dissemination Agent shall be the State Treasurer.

SECTION 8. Amendment; Waiver. Notwithstanding any other provision of this Disclosure Certificate, the State Treasurer may amend or waive any provision of this Disclosure Certificate, provided that the following conditions are satisfied:

(a) If the amendment or waiver relates to the provisions of Section 3(a), 4, 5(a), or 8, it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature or status of an obligated person with respect to the Bonds, or the type of business conducted;

(b) The undertaking, as amended or taking into account such waiver, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the original issuance of the Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and

(c) The amendment or waiver either (i) is approved by the Holders of 60% of the Bonds outstanding or (ii) does not, in the opinion of nationally recognized bond counsel, materially impair the interests of the Holders or Beneficial Owners of the Bonds. The State also may amend this Disclosure Certificate without approval by the Holders to the extent permitted by rule, order or other official pronouncement of the Securities and Exchange Commission.

In the event of any amendment or waiver of a provision of this Disclosure Certificate, the State Treasurer shall describe such amendment in the next Annual Report, and shall include, as applicable, a narrative explanation of the reason for the amendment or waiver and its impact on the type (or, in the case of a change of accounting principles, on the presentation) of financial information or operating data being presented by the State. In addition, if the amendment relates to the accounting principles to be followed in preparing financial statements, (i) notice of such change shall be given in the same manner as for a Listed Event under Section 5(b), and (ii) the Annual Report for the year in which the change is made should present a comparison (in narrative form and also, if feasible, in quantitative form) between the financial statements as prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles.

SECTION 9. Additional Information. Nothing in this Disclosure Certificate shall be deemed to prevent the State Treasurer from disseminating any other information, using the means of dissemination set forth in this Disclosure Certificate or any other means of communication, or including any other information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Certificate. If the State Treasurer chooses to include any information in any Annual Report or notice of occurrence of a Listed Event in addition to that which is specifically required by this Disclosure Certificate, the State Treasurer shall not have any obligation under this Disclosure Certificate to update such information or include it in any Annual Report or future notice of occurrence of a Listed Event.

SECTION 10. Beneficiaries. This Disclosure Certificate shall inure solely to the benefit of the Holders and Beneficial Owners from time to time of the Bonds, and shall create no rights in any other person or entity (except the right of the Dissemination Agent or any Holder or Beneficial Owner to enforce the provisions of this Disclosure Certificate on behalf of the Holders). This Disclosure Certificate is not intended to create any monetary rights on behalf of any person based upon the Rule.

SECTION 11. Partial Invalidity. If any one or more of the agreements or covenants or portions thereof required hereby to be performed by or on the part of the State Treasurer shall be contrary to law, then such agreement or agreements, such covenant or covenants or such portions thereof shall be null and void and shall be deemed separable from the remaining agreements and covenants or portions thereof and shall in no way affect the validity hereof, and the Holders of the Bonds shall retain all the benefits afforded to them hereunder. The State Treasurer hereby declares that he would have executed and delivered this Disclosure Certificate and each and every other article, section, paragraph, subdivision, sentence, clause and phrase hereof irrespective of the fact that any one or more articles, sections, paragraphs, subdivisions, sentences, clauses or phrases hereof or the application thereof to any person or circumstance may be held to be unconstitutional, unenforceable or invalid.

SECTION 12. Governing Law. The laws of the State of California shall govern this Disclosure Certificate, the interpretation thereof and any right or liability arising hereunder. Any action or proceeding to enforce or interpret any provision of this Disclosure Certificate shall be brought, commenced or prosecuted in Sacramento County, California.

IN WITNESS WHEREOF, the State Treasurer has executed this Disclosure Certificate as of the date first above written.

By ______________________________________
Deputy State Treasurer
For State Treasurer, Philip Angelides

APPENDIX D

PROPOSED FORMS OF LEGAL OPINIONS

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FINAL OPINION OF EACH CO-BOND COUNSEL

[Closing Date]

$______________
State of California
Various Purpose General Obligation Bonds

____
(Final Opinion)

We have acted as co-bond counsel in connection with the issuance by the State of California (the "State") of $______________ aggregate principal amount of State of California Various Purpose General Obligation Bonds, issued as six separate series under four bond acts, identified in Schedule A hereto (the "Bonds"). The Bonds are authorized pursuant to the respective bond acts identified in Schedule A (collectively, the "Laws") and are issued pursuant to Part 3 of Division 4 of Title 2 of the California Government Code and to resolutions (the "Resolutions") adopted by the respective finance committees created under the Laws.

In such connection, we have examined the record of proceedings submitted to us relative to the issuance of the Bonds, including the Resolutions, the tax certificate of the State (the "Tax Certificate"), other certifications of the State, and such other documents and matters deemed necessary by us to render the opinions set forth herein, although in doing so, we have not undertaken to verify independently the accuracy of the factual matters represented, warranted or certified therein, and we have assumed the genuineness of all signatures thereto.

The opinions expressed herein are based upon an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted or events occurring after the date hereof. We have neither undertaken to determine, nor to inform any person, whether any such actions are taken or omitted or events do occur or whether any other matters come to our attention after the date hereof. Furthermore, we have assumed compliance with the agreements and covenants contained in the Resolutions and the Tax Certificate, including (without limitation) agreements and covenants compliance with which is necessary to assure that future actions, omissions or events will not cause interest on the Bonds to be included in gross income for federal income tax purposes.

We call attention to the fact that the rights and obligations under the Bonds, the Resolutions and the Tax Certificate may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases, and to the limitations contained in State law regarding legal remedies against the State. Finally, we undertake no responsibility for the accuracy, completeness or fairness of the Official Statement or other offering material relating to the Bonds and express no opinion with respect thereto.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof, we are of the following opinions:

1. The State has lawful authority for the issuance of the Bonds, and the Bonds constitute the legal, valid and binding general obligations of the State payable in accordance with the Law from the

General Fund of the State. The full faith and credit of the State of California are pledged to the punctual payment of the principal of and interest on the Bonds.

2. Interest on the Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 and is exempt from California personal income taxes. Interest on the Bonds is not a specific preference item for purposes of calculating the federal individual or corporate alternative minimum taxes, although we observe that it is included in adjusted current earnings in calculating corporate alternative minimum taxable income. We express no opinion regarding any other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest on, the Bonds.

Very truly yours,

Schedule A

$__________ principal amount of State of California Class Size Reduction Kindergarten-University Public Education Facilities Bonds, Series AT, authorized by the State School Building Finance Committee under the Class Size Reduction Kindergarten-University Public Education Facilities Bond Act of 1998.

$__________ principal amount of State of California Class Size Reduction Kindergarten-University Public Education Facilities Bonds, Series AU, authorized by the Higher Education Facilities Finance Committee under the Class Size Reduction Kindergarten-University Public Education Facilities Bond Act of 1998.

$______ principal amount of State of California Kindergarten-University Public Education Facilities Bonds, Series G, authorized by the Higher Education Facilities Finance Committee under the Kindergarten-University Public Education Facilities Bond Act of 2002.

$______ principal amount of State of California Kindergarten-University Public Education Facilities Bonds, Series H, authorized by the State School Building Finance Committee under the Kindergarten-University Public Education Facilities Bond Act of 2002.

$__________ principal amount of State of California New Prison Construction Bonds, Series AA, authorized by the 1986 Prison Construction Committee under the New Prison Construction Bond Act of 1986.

$______ principal amount of State of California Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Bonds, Series J, authorized by the Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Finance Committee under the Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Act.

OPINION OF THE ATTORNEY GENERAL

[Closing Date]

The Honorable Philip Angelides
State Treasurer
Sacramento, California

$______________
State of California
Various Purpose General Obligation Bonds

____

Final Opinion

Honorable Philip Angelides:

We have acted as counsel to the State of California (the "State") in connection with the issuance by the State of $______________ aggregate principal amount of State of California Various Purpose General Obligation Bonds, dated April 1, 2004, issued as six separate series under four bond acts, all identified in Schedule A hereto, which is incorporated by reference (collectively, the "Bonds"). The Bonds are authorized pursuant to the respective bond acts identified in Schedule A (collectively, the "Laws") and are issued pursuant to Part 3 of Division 4 of Title 2 of the California Government Code and to resolutions (the "Resolutions") adopted by the respective finance committees created under the Laws.

In such connection, we have examined the record of proceedings submitted to us relative to the issuance of the Bonds, including the Resolutions, certifications of the State, and such other documents and matters deemed necessary by us to render the opinions set forth herein, although in doing so, we have not undertaken to verify independently the accuracy of the factual matters represented, warranted or certified therein, and we have assumed the genuineness of all signatures thereto.

The opinions expressed herein are based upon an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted or events occurring after the date hereof.

We have neither undertaken to determine, nor to inform any person, whether any such actions are taken or omitted or events do occur or whether any other matters come to our attention after the date hereof. Furthermore, we have assumed compliance with the agreements and covenants contained in the Resolutions. We call attention to the fact that the rights and obligations under the Bonds and the Resolutions may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases, and to the limitations contained in State law regarding legal remedies against the State. We express no opinion as to whether interest on the Bonds is excluded from gross income for federal income tax purposes or exempt from State of California personal income taxes or as to any other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest on, the Bonds. Finally, we undertake no responsibility for the accuracy, completeness or fairness of the Official Statement dated April ___, 2004, or other offering material relating to the Bonds and express no opinion with respect thereto.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof, we are of the opinion that the State has lawful authority for the issuance of the Bonds, and the Bonds constitute the legal, valid and binding general obligations of the State payable in accordance with the Laws from the General Fund of the State. The full faith and credit of the State of California are pledged to the punctual payment of the principal of and interest on the Bonds.

Sincerely,

Deputy Attorney General

For BILL LOCKYER
Attorney General

Schedule A

$__________ principal amount of State of California Class Size Reduction Kindergarten-University Public Education Facilities Bonds, Series AT, authorized by the State School Building Finance Committee under the Class Size Reduction Kindergarten-University Public Education Facilities Bond Act of 1998.

$__________ principal amount of State of California Class Size Reduction Kindergarten-University Public Education Facilities Bonds, Series AU, authorized by the Higher Education Facilities Finance Committee under the Class Size Reduction Kindergarten-University Public Education Facilities Bond Act of 1998.

$______ principal amount of State of California Kindergarten-University Public Education Facilities Bonds, Series G, authorized by the Higher Education Facilities Finance Committee under the Kindergarten-University Public Education Facilities Bond Act of 2002.

$______ principal amount of State of California Kindergarten-University Public Education Facilities Bonds, Series H, authorized by the State School Building Finance Committee under the Kindergarten-University Public Education Facilities Bond Act of 2002.

$__________ principal amount of State of California New Prison Construction Bonds, Series AA, authorized by the 1986 Prison Construction Committee under the New Prison Construction Bond Act of 1986.

$______ principal amount of State of California Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Bonds, Series J, authorized by the Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Finance Committee under the Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Act.

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